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Supreme Court, U.S.
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No. _____

In the
Supreme Court of the United States
October Term, 1993

Heartland Federal Savings and Loan Association,

Petitioner,

vs.

Briscoe Enterprises, Ltd., II,

Respondent.

Petition for Writ of Certiorari
to the United States Court of Appeals
for the Fifth Circuit

Petition for Writ of Certiorari

Douglas S. Lang
Deirdre Ruckman
Stacy R. Obenhaus*
GARDERE & WYNNE, L.L.P.
3000 Thanksgiving Tower
Dallas, Texas 75201
(214) 999-3000

Attorneys for Petitioner
*Counsel of Record

QUESTIONS PRESENTED

The questions presented involve confirmation by a bankruptcy court of a "cramdown" plan of reorganization pursuant to 11 U.S.C.A. § 1129(b). The court of appeals affirmed the bankruptcy court's confirmation of the plan in this case.

1. In order to establish the elements necessary to obtain confirmation of a cramdown plan of reorganization under 11 U.S.C.A. § 1129(b), is the proponent of the plan bound by a *clear and convincing evidence* standard of proof or by a *preponderance of the evidence* standard?

2. May the court of appeals, in determining whether a cramdown plan of reorganization is "fair and equitable" under 11 U.S.C.A. § 1129(b), place on a creditor opposing the plan the burden of showing that the proposed plan is *not* fair and equitable?

3. Does 11 U.S.C.A. § 1122 permit a court to confirm a plan of reorganization which places unsecured claims in separate classes while nevertheless giving them identical treatment?

LIST OF PARTIES

The following is a list of all of the parties to the proceeding in the United States Court of Appeals for the Fifth Circuit, whose judgment is sought to be reviewed:

Appellant:
Briscoe Enterprises, Ltd., II

Appellee:
Heartland Federal Savings and Loan Association

Heartland Federal Savings and Loan Association has the following parent companies or subsidiaries within the meaning of Supreme Court Rule 29.1:

None.

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TO THE UNITED STATES SUPREME COURT:

Heartland Federal Savings and Loan Association asks this court to issue a writ of certiorari to review the opinion issued July 13, 1993, by the United States Court of Appeals for the Fifth Circuit.

OPINIONS AND JUDGMENTS BELOW

Petitioner has reproduced in a separate appendix the opinions and judgments which the courts below have issued. The opinions and judgments are as follows:

Briscoe Enterprises, Ltd., II v. Heartland Federal Savings and Loan Association (In re Briscoe Partnership II, Ltd.), 994 F.2d 1160 (5th Cir. 1993) (appeal from the district court).

Heartland Federal Savings and Loan Association v. Briscoe Enterprises, Ltd., II, 138 Bankr. 795 (N.D. Tex. 1992) (on appeal from the bankruptcy court).

In re Briscoe Enterprises, Ltd., II, No. 489-44447-MT-11 (Bankr. N.D. Tex. Apr. 23, 1991) (original decision).

JURISDICTION

Briscoe filed a petition for relief under chapter 11 of the United States Bankruptcy Code, and the bankruptcy court had jurisdiction to entertain that petition pursuant to 28 U.S.C.A. § 157 (West 1993).

The court of appeals issued its opinion on July 13, 1993. The court of appeals denied Heartland's petition for rehearing on August 16, 1993. This court has jurisdiction, pursuant to 28 U.S.C.A. § 1254(1) (West 1993), to review the decision of the court of appeals.

STATUTES INVOLVED

11 U.S.C.A. § 1122 (West 1993):

(a) Except as provided in subsection (b) of this section, a plan may place a claim or an interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class.

(b) A plan may designate a separate class of claims consisting only of every unsecured claim that is less than or reduced to an amount that the court approves as reasonable and necessary for administrative convenience.

11 U.S.C.A. § 1129(a)(8), (10) (West 1993):

(a) The court shall confirm a plan only if all of the following requirements are met:

. . .

(8) With respect to each class of claims or interests —

(A) such class has accepted the plan; or

(B) such class is not impaired under the plan.

. . . .

(10) If a class of claims is impaired under the plan, at least one class of claims that is impaired under the plan has accepted the plan, determined without including any acceptance of the plan by any insider.

11 U.S.C.A. § 1129(b)(1), (2)(A) (West 1993):

(1) Notwithstanding section 510(a) of this title, if all of the applicable requirements of subsection (a) of this section other than paragraph (8) are met with respect to a plan, the court, on request of the proponent of the plan, shall confirm the plan notwithstanding the requirements of such paragraph if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.

(2) For the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements:

(A) With respect to a class of secured claims, the plan provides—

(i)(I) that the holders of such claims retain the liens securing such claims, whether the property subject to such liens is retained by the debtor or transferred to another entity, to the extent of the allowed amount of such claims; and

(II) that each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property;

(ii) for the sale, subject to section 363(k) of this title, of any property that is subject to the liens securing such claims, free and clear of such liens, with such liens to attach to the proceeds of such sale, and the treatment of such liens on proceeds under clause (i) or (iii) of this subparagraph; or

(iii) for the realization by such holders of the indubitable equivalent of such claims.

STATEMENT OF THE CASE

Briscoe Enterprises, Ltd., II, is a limited partnership formed to develop the Regalridge apartment complex in Fort Worth, Texas. Briscoe built Regalridge with financing from Heartland Federal Savings and Loan Association and the City of Fort Worth. Heartland loaned $18.7 million; the City loaned $7 million. The City's lien on Briscoe's property was junior to that of Heartland. In 1988 Briscoe began missing payments on the loans, and it subsequently filed for chapter 11 bankruptcy protection.

In the bankruptcy court Briscoe ultimately proposed a fourth amended plan of reorganization which divided the creditors' claims and interests into six classes:

Class 1 - allowed administrative claims.
Class 2 - allowed priority claims.
Class 3 - allowed unsecured claim of City of Fort Worth.
Class 4 - allowed secured claim of Heartland.
Class 5 - allowed unsecured claims.
Class 6 - holders of interests in Briscoe.

The bankruptcy court assigned the apartment property, Briscoe's principal asset, a value of $8.2 million, and that became the amount of Heartland's allowed secured claim in Class 4. Heartland's remaining $10 million claim was classified in Class 5 with the claims of other unsecured creditors. Class 4 was thus an impaired class, consisting solely of Heartland's secured claim. The City's unsecured $7 million claim was the sole claim classified in Class 3. However, the plan classified all other allowed unsecured claims in Class 5, and those claims were treated the same as the City's $7 million Class 3 unsecured claim.

1. The "preponderance of the evidence" standard.

Because Heartland's impaired Class 4 claim voted against the plan, the bankruptcy court could not confirm the plan unless Briscoe established that the plan met the "cramdown" requirements of 11 U.S.C.A. § 1129(b). Among other things, this meant that Briscoe had to show that the plan was "fair and equitable" as to each impaired class that had not accepted the plan. Thus, in this case Briscoe had to show that the plan was "fair and equitable" as to Heartland.

The bankruptcy court held a hearing on whether to confirm the plan, and it subsequently issued findings of fact and an order confirming the plan. Heartland filed an appeal from that order, and the district court reversed. The court ruled that a "clear and convincing evidence" standard was the correct standard of proof. The court concluded, however, that whether it applied a "clear and convincing" standard or a "preponderance of the evidence" standard, Briscoe had not satisfied its burden of showing that the plan was "fair and equitable" to Heartland under section 1129(b).

The court of appeals disagreed. Relying on *Grogan v. Garner*, 498 U.S. 279 (1991) and *Addington v. Texas*, 441 U.S. 418 (1979), it concluded that the "preponderance of the evidence" standard was the appropriate standard of proof for a cramdown plan of reorganization. 994 F.2d 1165. The court determined that Briscoe had proved all the elements of its case under that standard. It noted, however, that "this is a case in which the plan would not pass a clear and convincing standard." 994 F.2d at 1164.

2. The "fair and equitable" requirement.

The plan sets up a trust to manage the apartment property, and provides for payment of Heartland's $8.2 million secured claim through funds generated from the operation of the apartment over the next fifteen years. The plan contemplates payments in monthly installments of principal and interest, as though amortized over a 30 year period, at 10.25% interest. However, at the end of the fifteen year period only 20% of the principal would be paid. The remaining principal is to be paid in full in a single balloon payment made upon sale of the property or on the expiration of the fifteen year period, whichever occurs first.

In its findings of fact the bankruptcy court stated that the plan "has a marginal prospect of success," yet the court concluded that because the plan included the above terms for repayment of Heartland, the plan satisfied the "fair and equitable" requirements of 11 U.S.C.A. § 1129(b).

The district court disagreed. It determined that Briscoe had "failed to show, what the value of Regalridge will be in fifteen years, that there is any prospect for the sale or refinancing of Regalridge, or who the purchaser or refinancer might be." The district court also concluded that Briscoe had failed to sustain its burden even under a "preponderance of the evidence" standard.

The court of appeals did not cite to evidence from the record supporting this part of Briscoe's case. In fact, the court nowhere answered the district court's objections by expressly setting forth the specific evidence that Briscoe had offered to satisfy its burden of proof on this issue. Instead, the court asserted that "when the balloon is due,

either the property will be sold which will provide the balloon or refinancing will be possible." 994 F.2d at 1169. In the absence of evidence in the bankruptcy court record to support this assertion, the court argued that "[t]here is no evidence that the property will decline in value." *Id.* The court did recognize that "[e]stimating property values fifteen years hence is inherently speculative," but it said that "[i]t is reasonable to assume that the property itself will provide the source for the balloon payment." *Id.* Based on this assumption, the court of appeals found that this plan satisfied the "fair and equitable" requirement of section 1129(b).

3. Gerrymandering the City's unsecured claim.

The bankruptcy court found that a reasonable basis existed for separate classification of the City's unsecured Class 3 claim from the claims of other unsecured creditors in Class 5. The district court concluded that no evidence supported that finding. The court of appeals, while noting that the City's Class 3 unsecured claim was treated just like that of unsecured creditors in Class 5, concluded that good business reasons supported separate classification of the City's claim from the other unsecured creditor claims. 994 F.2d 1167. The court thereby affirmed the separate classification of the City's unsecured claim from the claims of the other unsecured creditors.

Pursuant to 11 U.S.C. § 1129(a)(10), if a class of claims is impaired under the plan, then at least one class of claims that is impaired must vote to accept the plan. Heartland voted its claim against the plan; the City voted for it. By placing the City's unsecured claim in a class by itself, Briscoe made certain that at least one impaired class would vote to accept the plan.

ARGUMENT

I. The decision to disregard the "clear and convincing evidence" standard will lead to confusion among the lower courts as to the applicable standard of proof in similar bankruptcy cases.

In deciding that *Grogan v. Garner* mandated the use of the "preponderance of the evidence" standard in order to confirm a "cramdown" plan of reorganization, the court of appeals put into question a substantial amount of case law from bankruptcy courts in other circuits. Until this decision, bankruptcy courts had overwhelmingly confirmed the application of the traditional "clear and convincing evidence" standard of proof in a "cramdown" confirmation hearing. *See In re Birdneck Apartment Assoc., II, L.P.*, 156 Bankr. 499, 507 (Bankr. E.D. Va. 1993); *In re S.A.B.T.C. Townhouse Ass'n, Inc.*, 152 Bankr. 1005, 1007-08 (Bankr. M.D. Fla. 1993); *Imperial Bank v. Tri-Growth Centre City, Ltd. (In re Tri-Growth Centre City, Ltd.)*, 136 Bankr. 848, 852 (Bankr. S.D. Cal. 1992); *In re Tallahassee Assoc., L.P.*, 132 Bankr. 712, 718 (Bankr. W.D. Pa. 1991); *In re Future Energy Corp.*, 83 Bankr. 470, 481 (Bankr. S.D. Ohio 1988); *In re Agawam Creative Marketing Assoc., Inc.*, 63 Bankr. 612, 618-19 (Bankr. D. Mass. 1986); *In re Stoffel*, 41 Bankr. 390, 392 (Bankr. D. Minn. 1984).

Yet the court of appeals' decision merits review by this court not only because of the potential for confusion regarding the appropriate standard of proof, but because the court's decision places in question the application of the "clear and convincing evidence" standard of proof in other bankruptcy contexts.

For example, the "clear and convincing evidence" standard presently applies when a trustee seeks turnover of estate property under section 542(a) of the Code, *Evans v. Robbins*, 897 F.2d 966, 969 (8th Cir. 1990); *Gorenz v. Illinois Dep't of Agriculture*, 653 F.2d 1179, 1184 (7th Cir. 1981); when a creditor contests the debtor's amendment of schedules, *In re Yonikus*, 996 F.2d 866, 872 (7th Cir. 1993); when a debtor seeks to rebut proof of a bad faith filing of the petition, *In re McCormick Road Assoc.*, 127 Bankr. 410, 416 (N.D. Ill. 1991); when a creditor seeks the appointment of a trustee under section 1104(a), *In re Mako, Inc.*, 102 Bankr. 809, 812 (Bankr. E.D. Okla. 1988); when a junior lienholder raises the defense of marshaling of assets, *In re Vermont Toy Works, Inc.*, 135 Bankr. 762, 766 (D. Vt. 1991); and when a creditor seeks to overcome the presumption of proper mailing of notice of bar dates, *In re Bucknum*, 951 F.2d 204, 207 (9th Cir. 1991).

The risk of confusion as to the proper standard of proof in these other bankruptcy contexts arises because of the broad reading which the court of appeals gave to this Court's decision in *Grogan v. Garner*.

Though the district court read *Grogan v. Garner* as applicable only to proceedings to determine whether debts were dischargeable, the court of appeals said this reading was too narrow. It focused on this Court's conclusion in *Grogan v. Garner* that Congressional silence with regard to the standard of proof in dischargeability proceedings was inconsistent with the view that Congress had intended to mandate a higher standard of proof in such cases. While that one factor, standing alone, might weigh against requiring "clear and convincing evidence" in the present case, this Court emphasized other factors as well, including that a higher standard of proof would increase the burden

of creditors whose state's laws imposed the preponderance of the evidence standard; that section 523 groups together the exceptions to discharge (suggesting that Congress did not intend for different standards to apply to the different exceptions); and that section 523 required a balancing of the "fresh start" policy with the interests of creditors seeking to recover a variety of debts, including alimony, taxes, and damages for fraud. 498 U.S. at 283-88.

Disregarding these other important factors which are unique to dischargeability proceedings, the court of appeals read *Grogan v. Garner* quite broadly, relying for the most part on this Court's general discussion of the standard of proof question in *Addington v. Texas*, 441 U.S. 418 (1979).

In *Addington* this court noted that the "clear and convincing evidence" standard had been reserved for cases involving quasi-criminal wrongdoing such as fraud, where something more than the mere loss of money is at risk, or for cases that implicate important individual interests, such as deportation or denaturalization proceedings. 994 F.2d at 1164-65. Finding no important liberty interests at stake with regard to Heartland's position as a secured creditor, and noting Congressional silence regarding the standard of proof under section 1129(b), the court of appeals declined to follow the virtually unanimous approach to this issue which the bankruptcy courts had taken.

If the silence of Congress and the absence of these important liberty interests constitute the cornerstone for application of a "clear and convincing evidence" standard, then the bankruptcy courts have little basis for applying that standard in any of the many contexts in which they have traditionally applied that standard.

Even outside the bankruptcy context, courts have not applied the "clear and convincing evidence" standard so narrowly, applying it in a number of instances in which liberty interests are not at risk, but important property rights are. *See Armistead v. Vernitron Corp.*, 944 F.2d 1287, 1295 (6th Cir. 1991) (reformation of contract); *Columbus-America Discovery Group v. Atlantic Mut. Ins. Co.*, 974 F.2d 450, 464 (5th Cir. 1992), *cert. denied*, 113 S. Ct. 1625 (1993) (abandonment of estate property); *Amoco Prod. Co. v. United States*, 852 F.2d 1574, 1580 (10th Cir. 1988) (quieting title to property).

Faced with an interstate water rights dispute in *Colorado v. New Mexico*, 467 U.S. 310 (1984), this Court reasoned that the clear and convincing evidence standard "accommodates society's competing interest in increasing the stability of property rights and in putting resources to their most efficient uses." *Id.* at 317. With regard to patent rights, the Federal Circuit has decided that the presumption of patent validity is so strong that only clear and convincing evidence will overcome that presumption. *See Price v. Symsek*, 988 F.2d 1187, 1191-92 (Fed. Cir. 1993). Thus, certain property rights are important enough that the courts, by application of the clear and convincing standard, regularly shift the risk of an erroneous decision to the one wishing to take away those rights.

The bankruptcy courts had good reason to require "clear and convincing evidence" of each of the elements necessary to confirm a "cramdown" plan of reorganization. Section 1129(a) allows impaired classes to object to the plan and thereby prevent confirmation, except where the proponent proves that the plan is "fair and equitable." The three alternative requirements for satisfying the "fair and equitable" test are only minimum requirements. *See*

11 U.S.C.A. § 1129(b)(2)(A) (West 1993). In establishing only minimum requirements, the Code left the bankruptcy courts with the duty to apply traditional equitable rules and principles in deciding whether to permit the plan to override the creditors' objections to what is frequently a drastic alteration of the creditors' state law rights. The court of appeals in this case long ago affirmed that a party had to satisfy the "clear and convincing" standard in order to obtain approval of a "cram down" reorganization. *See Atlantic Coast Line Ry. v. St. Joe Paper Co.*, 179 F.2d 538, 544 (5th Cir.) (requiring "clear and convincing proof that the provisions of the plan are fair and equitable" under former Bankruptcy Act), *cert. denied*, 339 U.S. 929 (1950).

The requirement of "clear and convincing" evidence arose in the courts of equity. *See* Note, *Appellate Review in the Federal Courts of Findings Requiring More than a Preponderance of the Evidence*, 60 Harv. L. Rev. 111, 112 (1946). Courts still apply this standard where a party seeks equitable relief. *See, e.g., Rentenbach Eng'g Co. v. General Realty, Ltd.*, 707 S.W.2d 524, 527 (Tenn. Ct. App. 1985); *Crompton v. Bruce*, 669 P.2d 930, 934 (Wyo. 1983); *Grabowski v. Grabowski*, 120 N.H. 745, 422 A.2d 1040, 1042 (1980). The bankruptcy courts properly relied on the established traditions of equity jurisprudence in giving effect to Congress's decision to allow a "cramdown" only where a plan's proponent showed by clear and convincing evidence that the plan was fair and equitable to objecting, impaired creditors.

The court of appeals has thus removed from the bankruptcy courts the power the Code gave them to apply the "fair and equitable" standard so as to prevent secured lenders — who have underwritten the debtor's activities — from having their interests swept lightly under the rug.

II. The court of appeals may not shift the burden to an opponent of a cramdown plan of reorganization to show that the plan is not "fair and equitable."

Briscoe, as the proponent of this cramdown plan of reorganization, had the burden of establishing all elements necessary to permit confirmation of the plan under section 1129. *See, e.g., In re Richard Buick, Inc.*, 126 Bankr. 840, 851 (Bankr. E.D. Pa. 1991); *In re Apple Tree Partners, L.P.*, 131 Bankr. 380, 393 (Bankr. W.D. Tenn. 1991); *In re Rusty Jones*, 110 Bankr. 362, 373 (Bankr. N.D. Ill. 1990). The court of appeals decided that the balloon payment which the plan provided satisfied the requirement under section 1129(b)(2) that the plan be "fair and equitable." 994 F.2d at 1168-69. In doing so, the court expressly relied on an assumption rather than on facts Briscoe had proved in the bankruptcy court. In addition, the court focused on facts which it said Heartland had failed to show, rather than on any facts Briscoe proved. The court thereby improperly placed on Heartland the burden of having to *disprove* the "fair and equitable" requirement.

Briscoe chose to establish the fair and equitable requirement under section 1129(b)(2)(A)(i), which is one of the three alternative minimum requirements for proving that the plan is "fair and equitable" under section 1129(b). Subsection (b)(2)(A)(i) requires that the secured creditor retain its lien on the property and receive "deferred cash payments totalling at least the allowed amount of such claim." In this case, Heartland would receive payments for a fifteen year period, at the end of which only 20 percent of the loan would be paid. At the end of this fifteen year period, Heartland would be paid the remaining 80 percent of its loan in one balloon payment.

The court explained why it felt this scheme was fair and equitable: "It is reasonable to assume that the property itself will provide the source for the balloon payment. There is no evidence that the property will decline in value . . . [T]he evidence did not suggest that the property would decline in value so that the debtor would be unable to pay Heartland its remaining principal." 994 F.2d at 1169.

Because Briscoe had the burden of proof on this issue, the question is not whether evidence showed that the property would decline in value in fifteen years. The issue is whether Briscoe showed that in fifteen years the property would have retained sufficient value to satisfy the balloon payment. Briscoe did not introduce such evidence. In fact, Briscoe presented no evidence as to the value of the property in fifteen years. Thus, there was simply no evidence from which to conclude one way or the other that the value of the property would rise or decline.

The court of appeals aptly noted in this case that "[e]stimating property values fifteen years hence is inherently speculative . . ." 994 F.2d at 1169. For this reason the majority of courts addressing this issue have held that balloon payments are rarely acceptable. *See In re Cranberry Hill Assoc., Ltd. Partnership*, 150 Bankr. 289, 291 (Bankr. D. Mass. 1993) (holding a balloon payment in nine years to be "far from certain"); *In re French Quarters East, L.P.*, 148 Bankr. 910, 911 (Bankr. W.D. Mo. 1992) (rejecting balloon payment in ten years); *In re M & S Assoc., Ltd.*, 138 Bankr. 845, 851-52 (Bankr. W.D. Tex. 1992) (confirmation of the plan, which included provisions for balloon payment, would allow the debtor to postpone the inevitable and gamble with secured creditor's money); *In re Pelham Street Assoc.*, 134 Bankr. 700, 701 (Bankr.

D.R.I. 1991) (stating that plan with five year balloon payment was "pie in the sky, and no secured creditor should be required to depend on such illusory pie"); *In re Lakeside Global II, Ltd*, 116 Bankr. 499, 514 (Bankr. S.D. Tex. 1989) (refusing to confirm a plan where satisfaction of balloon payment in three years was speculative).

This court should therefore make clear that under section 1129(b) a court of appeals cannot confirm a plan of reorganization based on assumptions or based on the failure of an opponent of the plan to show, in the absence of evidence proving the "fair and equitable" requirement, that the plan is not fair and equitable.

III. Congress did not intend that courts be able to gerrymander an impaired class so as to obtain an affirmative vote for a plan.

Section 1129(a)(10) of the Code provides that if a class of claims is impaired under the plan, the court may not confirm the plan unless at least one class of impaired claims votes to accept the plan. In this case, the plan gerrymandered an impaired class, in a manner contrary to section 1122, in order to create an impaired class which would accept the plan.

Specifically, the unsecured claim of the City was placed in class 3, while the unsecured claim of Heartland and the trade unsecured creditors were put in class 5. If the City's claim had remained with the other unsecured creditors' claims in class 5, then no impaired class would have accepted the plan. Class 5 voted against the plan, and the City's claim would not have changed that result.

However, the City's claim was in its own class, and it voted to accept the plan. That acceptance allowed the plan to satisfy section 1129(a)(10).

The court of appeals noted that "all the unsecured creditors will receive the same treatment." 994 F.2d at 1166. In a recent decision, the court took the opposite approach. In *In re Greystone III Joint Venture (Phoenix Mutual Life Ins. Co. v. Greystone III Joint Venture)*, 948 F.2d 134 (5th Cir. 1992), the court reversed a bankruptcy court order which confirmed a plan of reorganization. It held that under 11 U.S.C.A. § 1122 a plan may not classify similar claims differently simply in order to gerrymander an affirmative vote on a reorganization plan. *Id.* at 139. The court noted that separate classification of similar claims might be justified based on "good business reasons" but that such business reasons would only be valid if the different classes received different treatment under the plan. *Id.* at 141.

Other courts followed *Greystone*. *See, e.g., In re Bryson Properties, XVIII*, 961 F.2d 496, 502 (4th Cir.), *cert. denied*, 113 S. Ct. 191 (1992). However, in this case the court of appeals strayed from *Greystone* and indicated that classification of similar claims which are given identical treatment under the plan is not per se improper. By this petition, Heartland asks this court to hold that when the bankruptcy court classifies similar claims separately, the plan must also treat those claims differently. If the plan divides claims into separate classes but provides the same treatment, and if one of these classes is the only impaired class to vote for the plan, then the plan has improperly gerrymandered an impaired class solely in order to obtain an affirmative vote to satisfy section 1129(a)(10).

CONCLUSION

For these reasons, this court should grant this petition for writ of certiorari.

Respectfully submitted,

Douglas S. Lang
Deirdre Ruckman
Stacy R. Obenhaus*
GARDERE & WYNNE
3000 Thanksgiving Tower
Dallas, Texas 75201
(214) 999-3000

Attorneys for Petitioner
*Counsel of Record

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No. _____

In the Supreme Court of the United States
October Term, 1993

Heartland Federal Savings and Loan Association,

Petitioner,

vs.

Briscoe Enterprises, Ltd., II,

Respondent.

Petition for Writ of Certiorari
to the United States Court of Appeals
for the Fifth Circuit

Appendix to
Petition for Writ of Certiorari

Douglas S. Lang
Deirdre Ruckman
Stacy R. Obenhaus*
GARDERE & WYNNE, L.L.P.
3000 Thanksgiving Tower
Dallas, Texas 75201
(214) 999-3000

Attorneys for Petitioner
*Counsel of Record

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No. 92-1446

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

In re: Briscoe Enterprises, Ltd., II,
d/b/a Regalridge Apartments,

Debtor.

Heartland Federal Savings & Loan Association,

Appellee,

vs.

Briscoe Enterprises, Ltd., II,
d/b/a Regalridge Apartments,

Appellant.

July 13, 1993

Before Wisdom and Duhe, Circuit Judges, and Doherty,* District Judge.

*District Judge of the Western District of Louisiana, sitting by designation.

Wisdom, Circuit Judge:

This bankruptcy case requires the Court to confront some very difficult problems associated with a Chapter 11 "cramdown" reorganization.[1] We agree with the Bankruptcy court's approval of the reorganization plan; we REVERSE the District Court.

I.

The debtor, Briscoe Enterprises, Ltd., II, is a Texas limited partnership formed to develop a 784-unit apartment complex in a depressed section of Fort Worth. It is a low-to-moderate-income community, and about 25% of the residents received rental assistance from either the federal government or the City of Fort Worth. This complex, known as the Regalridge Square Apartments, was the sole asset of the limited partnership. Construction was in two phases. It was completed in early 1985. Financing was non-recourse and was from two sources: the predecessor of Heartland Federal Savings and Loan

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[1]"The cramdown provision allows a [reorganization] plan to be confirmed even if the necessary consents of each class [of creditors] are not obtained. The policy is that the public good is served by rehabilitations and a law that prevents creditors from getting immediate satisfaction but gives the creditor as much as the creditor could get upon liquidation and compensates him or her for the delay is proper to force upon creditors." 3 Daniel R. Cowans et al., *Cowans Bankruptcy Law and Practice* § 20.26 at 419 (1989 edition).

Association and the city of Fort Worth.[2] Heartland lent Briscoe $18.7 million. The city which had a lien junior to that of Heartland lent $7 million.

When the free-wheeling real estate ride of the mid-eighties ground to a halt, Briscoe began to miss its interest payments. Briscoe failed to make interest payments for the last three months of 1988 and entirely ceased servicing its debt to Heartland in July 1989. On December 29, 1989, Briscoe sought relief under 11 U.S.C. § 1101 et seq. (Chapter 11). Briscoe filed its first amended plan of reorganization on November 16, 1990 and its fourth on January 22, 1991. The fourth plan is the subject of this case.

On January 23, 1991, the bankruptcy court began hearings to consider the confirmation of the plan. The bankruptcy court held four days of hearings in January and one day in March. Eight witnesses appeared. The court, with counsel present, personally inspected the property. During these hearings, the bankruptcy court assigned a value to the property of $8.2 million. This was classified as a secured claim for Heartland. Heartland's remaining $10 million[3] and the city's $7 million became unsecured claims. Heartland objected, so that for the reorganization plan to be confirmed, it would have to pass the cramdown requirements of § 1129(b). The bankruptcy judge confirmed the plan on April 23, 1991.

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[2]The language of this opinion will treat Heartland as if it had made the initial loan.

[3]The bankruptcy court described Heartland's unsecured deficiency claim as "approximately $10 million".

Heartland appealed to the district court. The district court, without oral argument but in a lengthy opinion, reversed the bankruptcy court's confirmation on April 14, 1992.[4] Briscoe then appealed to this Court.

II.

The plan divides the claims and interests into six classes:

> "Class 1 consists of Allowed Administrative Claims.
> Class 2 consists of Allowed Priority Claims.
> Class 3 consists of the Allowed City Claim.
> Class 4 consists of the Allowed Heartland Claim.
> Class 5 consists of all Allowed Unsecured Claims asserted against the Debtor.
> Class 6 consists of holders of Interests in the Debtor."

The property is to be placed in a trust managed by three trustees. Heartland, the city, and the Fort Worth NAACP will each nominate a trustee. Heartland's claim was divided into a secured and an unsecured portion. The secured portion is to be paid in monthly installments of principal and interest as though amortized over thirty years with interest at a rate of 10.25%, the rate of interest in the loan. The secured claim is to be paid in full upon the sale

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[4] *In re Briscoe Enterprises Ltd., II*, 138 B.R. 795 (N.D. Tex. 1992).

of the property or the expiration of fifteen years, whichever shall first occur. At the end of fifteen years, 20% of the principal would be paid down. Heartland's unsecured claim is accorded the same treatment as the city's unsecured claim and the class 5 general unsecured creditors. These unsecured creditors are to receive periodic cash payments if net cash flow allows and the trustees determine that excess cash need not be reserved for any other purpose. The unsecured creditors would also benefit pro rata from any sale or refinancing of the property if there is an excess over Heartland's secured claim. The holders of class 6 interests will receive nothing and their interests are cancelled.[5]

III.

[1] The bankruptcy appellate process makes this Court the second level of appellate review. This Court, however, performs the identical task as the district court. We review the bankruptcy court's findings of fact under the clearly erroneous standard and its conclusions of law de novo.[6] We do benefit from the district court's thoughts on the matter, but as Judge Frank Johnson wrote for the Eleventh Circuit: "The amount of persuasive weight, if any, to be accorded the district court's conclusion . . . is entirely subject to our discretion."[7]

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[5]This appears to fulfill the requirements of § 1123(a)(3).

[6]*Matter of Bennett*, 970 F.2d 138, 139 (5th Cir. 1992).

[7]*In re Sublett*, 895 F.2d 1381, 1384 n.5 (11th Cir. 1990).

IV.[5]

A. *The Debtor's Standard of Proof.*

The first question that we need to resolve is the debtor's standard of proof in proving that the reorganization is confirmable under § 1129(a) and whether the fact that this is a § 1129(b) cramdown affects the standard.

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[5]Professor Elizabeth Warren was consulted as an outside expert in compliance with (A)(4) of Canon 3 of the Code of Judicial Conduct for United States Judges which in pertinent part provides: "A judge may obtain the advice of a disinterested expert on the law applicable to the proceeding before the judge if the judge gives notice to the parties of the person consulted and the substance of the advice, and affords the parties reasonable opportunity to respond." Justice Roger Traynor ended an article on appellate judging with the comment that: "There is no reason why courts should not request in complicated cases the disinterested expert opinion of scholars . . . We might well develop a tradition of regarding such public service as one of the most honorable responsibilities of the profession." Roger J. Traynor, *Badlands In An Appellate Judge's Realm of Reason*, 7 Utah L. Rev. 157, 170 (1960). Professor Warren is the Warren A. Schnader Professor of Commercial Law at the University of Pennsylvania and Robert Braucher Visiting Professor of Law at Harvard. She is the co-author (with Prof. Westbrook) of *The Law of Debtors and Creditors* (Little Brown 2nd ed. 1992) and is preparing a handbook for the Federal Judicial Center on Business Bankruptcy.

[2] The two options are proof by a preponderance of the evidence or by clear and convincing evidence. "Preponderance" means that it is more likely than not.[9] "Clear and convincing" is a higher standard and requires a high probability of success.[10]

A number of bankruptcy courts have used the clear and convincing standard in a cramdown, but in none of the cases have we found a satisfactory explanation why that is the appropriate standard.[11] A few hedge and state that the plan would fail under either standard.[12] This is exactly what the district court did in this case.[13] As we view it, however, this is a case in which the plan would not pass a clear and convincing standard, but, as will be discussed below, it was not clearly erroneous for the bankruptcy court to conclude that the plan was feasible and the cramdown fair and equitable under a preponderance standard.

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[9]*See e.g., In re Winship*, 397 U.S. 358, 371, 90 S. Ct. 1068, 1076, 25 L. Ed. 2d 368, 379 (1970) (Harlan, J., concurring).

[10]*See e.g., Aetna Insurance Co. v. Paddock*, 301 F.2d 807, 811 (5th Cir. 1962).

[11]*See e.g., In re Mcorp Financial, Inc.*, 137 B.R. 219, 225 (Bkrtcy. S.D. Tex. 1992) and cases cited therein.

[12]*See e.g., In re Rusty Jones, Inc.*, 110 B.R. 362, 373 (Bkrtcy. N.D. Ill. 1990).

[13]*Briscoe*, 138 B.R. at 805.

The United States Supreme Court has on several occasions discussed when particular standards of proof are applicable. Chief Justice Burger in *Addington v. Texas* spoke of the different factual settings which prompt a particular standard. "At one end of the spectrum is the typical civil case involving a monetary dispute between private parties."[14] In such a case the "plaintiff's burden of proof is a mere preponderance of the evidence".[15] At the other end of the spectrum is a criminal case. The nature of a criminal proceeding has led our legal system to require that the guilt of the accused be proved beyond a reasonable doubt. Between these two poles is some middle standard. "The intermediate standard, which usually employs some combination of the words 'clear,' and 'cogent,' and 'unequivocal,' and 'convincing,' is less commonly used, but nonetheless 'is no stranger to the civil law.'"[16] The Chief Justice noted that this standard had typically been employed in civil cases when "the interests at stake are deemed to be more substantial than mere loss of money".[17] He proceeded to cite several cases in which the Supreme Court had used the clear and convincing standard "to protect particularly important individual

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[14]*Addington v. Texas*, 441 U.S. 418, 423, 99 S. Ct 1804, 1807, 60 L. Ed. 2d 323 (1979).

[15]*Id.*

[16]*Addington* at 424, 99 S. Ct. at 1808 quoting *Woodby v. INS*, 385 U.S. 276, 285, 87 S. Ct. 483, 487, 17 L. Ed. 2d 362, 368 (1966).

[17]*Addington*, 441 U.S. at 424, 99 S. Ct. at 1808.

interests".[18] These concerned deportation and denationalization. *Addington*, itself, concerned involuntary commitment to a mental institution, and the Court rejected the suggestion that preponderance was the correct burden.

This case clearly does not fit within any of the above "liberty" categories. The Supreme Court, however, gives further guidance in several opinions in which it held that "clear and convincing" was the incorrect standard and that "preponderance" should be used. In *Herman & MacLean v. Huddleston*[19], Justice Marshall for the Supreme Court reversed this Court's conclusion that the clear and convincing standard was appropriate in a 10b-5 case, although the late Judge Rubin had suggested that because of its analogy to civil fraud and its effect on the defendant's reputation, the higher standard was the correct one. Justice Marshall's opinion relied on some older cases in which it seems that the Court contemplated only preponderance or reasonable doubt.[20] The Court unanimously refused, however, to depart from the preponderance standard although the case involved fraud. This may express a more restricted view of when clear and

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[18]*Id.*

[19]459 U.S. 375, 103 S. Ct. 683, 74 L. Ed. 2d 548 (1983).

[20]*U.S. v. Regan*, 232 U.S. 37, 34 S. Ct. 213, 58 L. Ed. 494 (1914) (preponderance is appropriate in a civil suit even though it involves proof of acts that expose a party to a criminal prosecution). *SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344, 64 S. Ct. 120, 88 L. Ed. 88 (1943) (preponderance is sufficient to establish fraud under § 17(a) of the 1933 Act).

convincing is appropriate than the *Addington* Court which noted that clear and convincing had often been used in civil cases involving fraud or "some other quasi-criminal wrongdoing".[21]

In 1991, the Supreme Court in *Grogan v. Garner*[22] reversed the Eight Circuit which had held that clear and convincing was the creditor's standard of proof to show that a debtor's debt was not dischargeable under 11 U.S.C. § 523(a) because it had been procured by fraud. The Court, after citing the "particularly important interests" language of *Huddleston* and *Addington*, observed that both the language of the statute and the statutory history were silent as to burden of proof. The Court viewed this silence as "inconsistent with the view that Congress intended to require a special, heightened standard of proof".[23] Moreover, the Court examined the conflicting interests and concluded that proof by a preponderance of the evidence would reflect "a fair balance" between the conflicting interests. [24]

[3] In this case, the district court found *Grogan* inapplicable because it involved dischargeability. Considering the other precedents and the process of the

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[21]*Addington*, 441 U.S. at 424, 99 S. Ct. at 1808, 60 L. Ed. 2d at 329.

[22]498 U.S. 279, 111 S. Ct. 654, 112 L. Ed. 2d 755 (1991).

[23]*Grogan* at 286, 111 S. Ct. at 659, 112 L. Ed. 2d at 764.

[24]*Grogan* at 287, 111 S. Ct. at 659, 112 L.Ed. 2d at 765.

Grogan Court, we find this to be too narrow a reading of *Grogan*. In this case, both § 1129 and the legislative history are silent as to the burden of proof. This case is solely about money. There are not even any quasi-liberty interests at stake. It is correct, of course, as Justice Brandeis noted during the depression in a case involving the significant alteration of farm mortgagees' rights, that the Bankruptcy laws are subject to the Takings clause.[25] The Code, however, has been the primary source of the creditors' protections, not the Fifth Amendment. Congress provides protections for creditors, and in many instances it allows debtors to impinge on creditor's state law rights. Bankruptcy frequently rewrites the secured creditor's state law bargain. An example of this is the automatic stay of § 362, as a result of which the creditor has lost the right of foreclosure. The calculation of claims under § 502 is another example of the Code rewriting the secured creditor's bargain. The combination of legislative silence, Supreme Court holdings, and the structure of the Code leads this Court to conclude that preponderance of the evidence is the debtor's appropriate standard of proof both under § 1129(a) and in a cramdown.[26]

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[25]*Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 55 S. Ct. 854, 79 L. Ed. 1593 (1935).

[26]Heartland suggests that because the word "indubitable" (meaning, according to Webster, "too evident to be doubted; unquestionable") is used in the fair and equitable requirement of § 1129(b), a cramdown requires more than preponderance. Heartland is confusing the issue. § 1129(b)(2)(A)(iii) states that "With respect to a class of secured claims, the plan provides . . . for the realization by such holders of the undubitable equivalent

B. *Feasibility of the Reorganization*

[4] As numerous courts have explained, "the court need not require a guarantee of success,"[27] which of course would be difficult to predict for any venture much less one emerging from chapter 11. "Only a reasonable assurance of commercial viability is required."[28] Our task is to determine whether it was clearly erroneous for the bankruptcy court to find that the plan provided a reasonable assurance of commercial viability by a preponderance of the evidence.

This case presents a difficult appellate review because the bankruptcy court has itself acknowledged that the reorganization has only a "marginal prospect of success". The district court paraphrased the familiar language from *Anderson v. Bessemer City* in which the Supreme Court reiterated that the clearly erroneous standard "does not entitle a reviewing court to reverse the finding of the trier of fact simply because it would have

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of such claims." Under this option, the debtor must show that the creditor will receive the indubitable equivalent of its claims by a preponderance of the evidence. The level of proof to show indubitability is not raised merely by the use of the word "indubitable". "Indubitable" modifies "equivalent" not "provides". Section F discusses the debtor's satisfaction of the fair and equitable requirement.

[27]*See e.g., In re Lakeside Global II*, 116 B.R. 499, 507 (Bkrtcy. S.D. Tex. 1989).

[28]*Id.*

decided the case differently."[29] It does not, however, appear to have taken these words to heart nor those of Justice Jackson to which the *Anderson* Court referred, who explained in the well-known antitrust case, *U.S. v. Yellow Cab*, [30] that "where there are two permissible views of the evidence, the fact finder's choice between them cannot be clearly erroneous".[31] The Anderson Court further explained that, "This is so even when the [finder of facts] findings do not rest on credibility determinations, but are based instead on physical or documentary evidence or inferences from other facts."[32]

The bankruptcy court found that the debtor could fund its debt service to Heartland and pay operating expenses out of its rental income. The bankruptcy court noted that occupancy had increased at the property during the pendency of this case from 55% to 85%, and that evidence suggested that occupancy would increase to 90%. The debtor's historic turnover rate is considerably less than its neighbors, and it requires a one-year lease and a security deposit. Although economic occupancy is less than physical occupancy because of promotions, there is no indication that this is more than a temporary occurrence. Heartland has further suggested that the debtor is unable to pay for necessary repairs. The bankruptcy court found

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[29]470 U.S. 564, 573, 105 S. Ct. 1504, 1511, 84 L. Ed. 2d 518, 528 (1985).

[30]338 U.S. 338, 70 S. Ct. 177, 94 L. Ed. 150 (1949).

[31]*Anderson*, 470 U.S. at 574, 105 S. Ct. at 1511 paraphrasing *Yellow Cab*, 338 U.S. at 342, 70 S. Ct. at 179.

[32]*Anderson*, 470 U.S. at 574, 105 S. Ct. at 1511.

that some of the repairs are urgent, and these could be funded from insurance proceeds. The rest could be delayed and paid out of cash flow. Although the bankruptcy court cautioned the debtor that it "will have to work diligently to make this Plan succeed", it found that there was a reasonable prospect for success and that the plan would not likely be followed by further reorganization or liquidation. True, some triers of fact *may* have found that the evidence tipped slightly against feasibility, but the bankruptcy court's finding that this plan was feasible cannot be characterized as clearly erroneous.

C. *Classification of Claims*

Heartland argues that the debtor's separate classification of the unsecured creditors violated § 1122.[33] Although all the unsecured creditors will receive the same treatment, classification matters because to effect a cramdown at least one impaired class must vote to accept the plan. If there was only one unsecured class, Heartland's ten million dollar claim would prevent the class from accepting the plan under § 1126, and cramdown

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[33]11 U.S.C. § 1122 provides:

(a) Except as provided in subsection (b) of this section, a plan may place a claim or an interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class.

(b) A plan may designate a separate class of claims consisting only of every unsecured claim that is less than or reduced to an amount that the court approves as reasonable and necessary for administrative convenience.

would not be allowed. We must determine therefore whether the bankruptcy court erred in permitting this separate classification.

Matter of *Greystone*[34] is a recent and leading case on classification of claims. The general rule of *Greystone* is that "thou shalt not classify similar claims differently in order to gerrymander an affirmative vote on a reorganization plan."[35] *Greystone*, however, recognized that there may be good business reasons to support separate classification. *Greystone* also noted that, "Whether there were any good business reasons to support the debtor's separate classification is a question of fact" and thus subject to clearly erroneous review.[36] The Court of Appeals for the Sixth Circuit in *U.S. Truck*[37] enunciated the business reason justification for separate classification. In *U.S. Truck*, the court allowed the debtor to place the Teamsters in a separate class because the Teamsters had "a different stake in the future viability of the reorganized company and [had] alternative means at its disposal for protecting its claim".[38] While the business justification was sufficient in *U.S. Truck*, it was not in *Greystone*, because there was no evidence that the debtor's ongoing business

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[34]*Matter of Greystone*, 948 F.2d 134 (5th Cir. 1991), *cert. denied*, ___ U.S. ___, 113 S. Ct. 72, 121 L. Ed. 2d 37 (1992).

[35]*Greystone* at 139.

[36]*Greystone* at 141 n.7.

[37]*In re U.S. Truck*, 800 F.2d 581 (6th Cir. 1986).

[38]*U.S. Truck* at 587.

would be affected if separate classification were not permitted.

[5] These two carefully considered opinions guide our discussion in this case. This city of Fort Worth is distinct from other creditors including Heartland. Not only does it have non-creditor interests relating to its urban housing program, but it contributes $20,000 a month in rental assistance. Heartland argues that the plan is not feasible because there is no assurance of continued rental assistance from the city. This argument suggests that the relationship with the city is essential to the continued operation of this housing complex. Its continuing contributions and interests make it distinct from Heartland and the trade creditors. We emphasize the narrowness of this holding. In many bankruptcies, the proffered reasons as in *Greystone* will be insufficient to warrant separate classification. Here it seems justified. Moreover, as Heartland nominates one of the three trustees, it has means for protecting its interests. Therefore, we hold that the bankruptcy court was not clearly erroneous in separately classifying the city's unsecured claim.

D. *The Good Faith Requirement*

[6] § 1129(a)(3) requires that the debtor propose the plan in good faith. This Court has held that, "Where the plan is proposed with the legitimate and honest purpose to reorganize and has a reasonable hope of success, the good faith requirement of section 1129(a)(3) is satisfied."[39] The bankruptcy court found good faith

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[39]*Matter of Sun Country Development, Inc.*, 764 F.2d 406, 408 (5th Cir. 1985).

because "the Plan provides a vehicle for restructuring the debt of the Property and preserving the Property for the benefit of both creditors and the Fort Worth community. Moreover, none of the interest holders of the Debtor will retain anything under the Plan." A plan may not be the one that the creditors would themselves design and may indeed not be confirmed and yet still pass the good faith requirement. This plan which the bankruptcy court did confirm and in which the debtor will not retain any equity interest satisfies the good faith requirement.

E. *The Best Interests of Creditors Test*

[7] § 1129(a)(7) requires that each holder of a claim in a class either accept the plan or receive at least as much as it would receive in a chapter 7 liquidation. Because only Heartland objects, our task is to determine whether it will receive as much under the plan in present value terms[40] as it would if the property were sold today. The bankruptcy court assigned a value of $8.2 million to the property. Assuming that the property could be sold today, that is the amount the court concluded that Heartland would receive, and that is all that Heartland would ever receive. Under the plan, Heartland will not only receive $8.2 million but could receive periodic payments towards its unsecured claim.[41] In addition, it will share in any appreciation in the property. We need

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[40]*In re Mortgage Investment Co. of El Paso, Texas*, 111 B.R. 604, 615 (Bkrtcy. W.D. Tex. 1990).

[41]The absolute priority rule is not implicated because no class junior to Heartland's dissenting unsecured class will receive or retain anything under the plan.

not concern ourselves with any additional benefits Heartland may receive, for § 1129(a)(7) requires only that Heartland receive the present value of $8.2 million. There is no evidence that the property will decline in value before Heartland is paid in full its $8.2 million secured claim, and as explained in the next section of this opinion, the interest rate fully compensates Heartland for the delay in payment. Heartland may wish to cut its losses now rather than wait and see if it may eventually receive more, but the rationale underlying Congressional establishment of the cramdown prevents the creditor from blocking a fair and feasible reorganization.

F. *The Fair and Equitable Requirement for a Cramdown.*

§ 1129(b) requires that a cramdown be fair and equitable.[42] The statute provides three alternative minimum requirements for the plan to be considered fair and equitable with regard to secured creditors:

1129(b)(2) For the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements:

(A) With respect to a class of secured claims, the plan provides —

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[42]For a recent discussion of the fair and equitable requirement *see* Jack Friedman, *What Courts Do To Secured Creditors In Chapter 11 Cram Down*, 14 Cardozo L. Rev. 1495 (1993).

> (i)(I) that the holders of such claims retain the lien securing such claims, whether the property subject to such lien is retained by the debtor or transferred to another entity, to the extent of the allowed amount of such claims; and
>
> (II) that each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a value, as of the effective date of the plan, of at least the value of such holder's interest in the estate's interest in such property;
>
> (ii) for the sale, subject to section 363(k) of this title, of any property that is subject to the lien securing such claims, free and clear of such lien, with such lien to attach to the proceeds of such sale, and the treatment of such lien on proceeds under clause (i) or (iii) of this subparagraph; or
>
> (iii) for the realization by such holders of the indubitable equivalent of such claims.

The bankruptcy court held the plan to be feasible under the first option. The district court reversed as it viewed the "indubitable equivalent" language as mandatory rather than as one of three options.[43]

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[43]The district court stated that, "'Fair and equitable' as used in the context of a cramdown means that, at a minimum, the secured creditor must receive the indubitable equivalent of his secured claim." *Briscoe* at 810.

[8] While this Court has held that simple technical compliance with one of the three options in 1129(b)(2)(A) may not necessarily satisfy the fair and equitable requirement,[44] it has not transformed the "or" in 1129(b)(2)(A) into an "and". As we hold that the plan satisfied 1129(b)(2)(A)(i), we need not attempt to decipher the meaning of "indubitable equivalent".[45]

1129(b)(2)(A)(i) requires that the secured creditor retain its lien and receive "deferred cash payments totaling at least the allowed amount of such claim". The district court was concerned that the plan did not adequately ensure that Heartland will retain its liens. We interpret the plan as ensuring that if the debtor fails to comply with its debt service obligations, Heartland would have the right to foreclose. The language about the "letter and spirit of the plan" is not intended to affect Heartland's right to foreclose if it does not get paid what it is due under the plan. Deferred cash payments consist of an appropriate

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[44]*Matter of D & F Construction, Inc.*, 865 F.2d 673, 675-76 (5th Cir. 1989). In that case, the plan's negative amortization required the secured creditor to contribute additional money to the plan for twelve years before principal would be repaid. The creditor's ability to foreclose during this period was also impaired. This Court assumed for purposes of the case that the requirements of 1129(b)(2)(A) had been "literally met."

[45]One author has commented that, "More has been written on indubitable equivalence with less effect than on almost any other area of bankruptcy law." Richard F. Broude, *Reorganization Under Chapter 11 of the Bankruptcy Code*, 13-24 (1986).

interest rate and an amortization of the principal which constitutes the secured claim.

[9, 10] We review a bankruptcy court's calculation of an appropriate interest rate for clear error.[46] Courts have used a wide variety of different rates as benchmarks in computing the appropriate interest rate (or discount rate as it is frequently termed) for the specific risk level in their cases.[47] In this case the bankruptcy court adopted the contract rate which was 10.25%. Numerous courts have chosen the contract rate if it seemed to be a good estimate as to the appropriate discount rate.[48] Often the contract rate will be an appropriate rate but reference to a similar maturity Treasury rate is instructive. The Treasury rate is helpful because it includes all necessary factors except the risk premium.[49] Treasury bonds with

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[46]*In re Bryson Properties XVIII*, 961 F.2d 496, 500 n.5 (4th Cir. 1992).

[47]A properly calculated interest rate should factor in the appropriate risk. *See e.g., In re Guildford Telecasters, Inc.*, 128 B.R. 622 (Bkrtcy. M.D.N.C. 1991); *In re Sherwood Square Associates*, 107 B.R. 872 (Bkrtcy. D. Md. 1989). C. Frank Carbineer's *Present Value in Bankruptcy: The Search for an Appropriate Cramdown Discount Rate*, 32 S.D.L. Rev. 42 (1987) is an excellent introduction to this subject.

[48]*See e.g., In re Monnier Bros.*, 755 F.2d 1336, 1339 (8th Cir. 1985); *Guildford* at 626.

[49]We assume that Treasury bonds as they are backed by the United States Government contain zero risk.

15 years to maturity (the term of this reorganization) were priced at around 6.4% in June 1993. A discount rate of 10.25% is more than 50% greater than the riskless rate. This risk premium is comparable with that of many "junk bonds". While it may in fact be too high a rate considering that we only reach this stage once the plan has been judged feasible,[50] it was not clearly erroneous for the bankruptcy court to find that this risk premium adequately compensates Heartland for not receiving its money today.

[11] Having found the interest rate to be acceptable, we must next consider the balloon payment. These two issues are interrelated for the balloon payment adds some measure of risk, but the interest rate appears adequate to cover this risk. Heartland and the district court suggest that allowing a balloon payment is unacceptable as there is no immediate indication from where the funds will come to pay off the balloon. As a general matter, many courts have held balloon payments to satisfy 1129(b).[51] It is reasonable to assume that the property itself will provide the source for the balloon payment. There is no evidence that the property will decline in value. Therefore, when the balloon is due, either the property will be sold which will provide the balloon or refinancing will be possible.[52] Estimating property values fifteen years hence is inherently speculative, but the evidence presented to the bankruptcy

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[50]*See In re Landmark at Plaza Park, Ltd.*, 7 B.R. 653, 658 n.8 (Bkrtcy. D.N.J. 1980).

[51]*See e.g., Bryson* at 501; *Guildford* at 627.

[52]This satisfies § 1123(a)(5) which requires that the plan provide adequate means for its implementation.

court did not suggest that the property would decline in value so that the debtor would be unable to pay Heartland its remaining principal. Therefore, we hold that the plan satisfies 1129(b)(2)(A)(i). No other factors in this case lead us to hold that compliance with 1129(b)(2)(A)(i) fails to satisfy the fair and equitable requirement. Accordingly, we affirm the bankruptcy court's holding that the plan is fair and equitable.

G. *Administrative Claims and Use of Cash Collateral.*

Heartland argues that the debtor impermissibly hired an appraiser, an architect, and a marketing consultant. The bankruptcy judge approved these nunc pro tunc. Heartland suggests that this is an impermissible use of cash collateral in violation of § 506(c), and that no exceptional circumstances warranted the nunc pro tunc order.

[12] We review the bankruptcy court's implicit finding of no violation of § 506(c) under the clearly erroneous standard.[53] Its nunc pro tunc order is reviewed for abuse of discretion.[54]

[13] Heartland is correct that this Court has denied a utility bill under § 506(c). In that case, however, this Court upheld a bankruptcy court's conclusion because it was not clearly erroneous to conclude that keeping the

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[53]*Matter of Delta Towers*, 924 F.2d 74, 77-78 (5th Cir. 1991).

[54]*Matter of Triangle Chemicals*, 697 F.2d 1280, 1288-89 (5th Cir. 1983).

lights on did not benefit the creditor of a bankrupt hotel, whose security interest was solely in the building and movables and had no interest in the operation. The district judge had reversed the bankruptcy judge, and this Court observed that while "there is evidence to support the district court's findings [that the utilities prevented the deterioration of the building and maintained the going concern value], the district court does not enjoy absolute freedom to make its own findings".[55] There is also considerable difference between utility expenses for a bankrupt hotel and hiring an appraiser, an architect, and a marketing consultant for an operating and expanding *apartment* complex in which the creditors have a considerable interest. Indeed, as the bankruptcy court used the appraiser's estimate and the occupancy rate increased after the architect and marketing consultant were hired, it does not seem clearly erroneous for the bankruptcy court to have permitted these expenses. The bankruptcy court found that the marketing consultant's fee of $23,000 was justified. We affirm that finding but urge prudence on the part of debtors and careful scrutiny on the part of bankruptcy courts to ensure that expenses are tailored carefully to the need.

As for these orders being nunc pro tunc, the equitable discretionary powers of the bankruptcy court are broad; in this situation the bankruptcy court did not abuse its discretion in granting these orders nunc pro tunc. These expenses were incurred during a period when the debtor's original counsel was forced to recuse itself as a result of a conflict and replacement representation had not

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[55]*Delta Towers* at 78.

yet been retained. Very soon after the debtor obtained substitute counsel, approval of the debtor's use and retention of these professionals was sought. Therefore, while again encouraging bankruptcy courts to examine carefully the grant of nunc pro tunc orders, we hold that in this case the bankruptcy court did not abuse its discretion.

V.

This is a difficult case and both the bankruptcy court and the district court are to be commended for their efforts. We REVERSE the district court and AFFIRM the bankruptcy court's confirmation of the plan and orders nunc pro tunc and wish the trustees good luck in reorganizing this property.

IN THE UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF TEXAS
FORT WORTH DIVISION

In re:	§	
	§	
Briscoe Enterprises Ltd., II,	§	
	§	
	§	Civil Action No.
Debtor.	§	4-91-457-A
	§	
Heartland Federal Savings and Loan Association,	§	
	§	(Consolidated with
	§	
Appellant,	§	Civil Action No.
	§	4-91-458-A,
vs.	§	Civil Action No.
	§	4-91-459-A,
Briscoe Enterprises Ltd., II,	§	Civil Action No.
	§	4-91-460-A,
	§	Civil Action No.
Appellee.	§	4-91-461-A)

FINAL JUDGMENT

Consistent with the memorandum and opinion of even date herewith,

The court ORDERS, ADJUDGES and DECREES that:

1. The bankruptcy court's findings of fact and conclusions of law Nos. 12, 13, 15, 17, 22, 26, 27, 31, 36, 37, 38, 41, 42 and 43 be, and are hereby, set aside;

2. The bankruptcy court's orders (a) confirming debtors fourth amended plan of reorganization, (b) employing and retaining James W. Daniels & Associates, Inc., as appraiser, and (c) employing and retaining John R. Horton, Inc., as architectural design and supervision company, and the ruling of the bankruptcy judge approving the employment of the marketing agent, nunc pro tunc, be, and are hereby, REVERSED; and

3. These consolidated actions be, and are hereby, REMANDED for further action consistent with the court's rulings in the memorandum opinion and order signed this date and with this final judgment.

SIGNED April 14, 1992.

s/John McBryde
John McBryde
United States District Judge

IN THE UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF TEXAS
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Briscoe Enterprises Ltd., II,	§	Civil Action No.
	§	4-91-460-A,
	§	Civil Action No.
Appellee.	§	4-91-461-A)

MEMORANDUM OPINION AND ORDER

This consolidated action encompasses appeals from five separate orders rendered by the United States Bankruptcy Court, Northern District of Texas, Fort Worth Division, the Honorable Massie Tillman presiding. The court, having reviewed the briefs of appellant, Heartland Federal Savings and Loan Association ("Heartland"), and appellee, Briscoe Enterprises Ltd., II ("Debtor"), the record on appeal and applicable authorities, makes the following determinations:

I.
Jurisdiction

The appeals are from orders entered by the bankruptcy court on April 24, 1991 (one order), January 25, 1991 (three orders), and January 24, 1991 (one order). This court's jurisdiction exists pursuant to 28 U.S.C. § 158(a).

II.
Undisputed Facts

Debtor, a Texas limited partnership, owns a 784-unit apartment complex known as the Regalridge Square Apartments ("Regalridge") in Fort Worth, Texas. Regalridge houses low to moderate income families, many of whom receive rent subsidies. Regalridge was constructed in two phases with financing provided by Heartland's predecessor. In connection with the development of each phase, debtor executed a non-recourse note in the original amount of $9.5 million dollars and a deed of trust granting a lien in that portion of the property then being developed. Heartland is the owner and holder of the notes and deeds of trust, dated April 11, 1983, and January 31, 1984, respectively. Additional financing of $3.5 million dollars for each phase was provided by the City of Fort Worth ("City"), which retained inferior liens in the property.

Debtor defaulted on its notes by failing to make interest payments in October, November, and December 1988. It entirely ceased servicing its debt to Heartland in July 1989.

III.
Proceedings

A voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code was filed by debtor on December 29, 1989; and, it filed its plan of reorganization on June 11, 1990. On August 17, 1990, debtor filed an unsigned copy of its proposed disclosure statement. It filed its first amended plan of reorganization on November 16, 1990. The plan was later modified by the filing of debtor's second amended plan of reorganization on December 12, 1990, third amended plan of reorganization on December 20, 1990, and fourth amended plan of reorganization on January 22, 1991. Debtor filed its first amended disclosure statement on November 16, 1990, second amended disclosure statement on December 12, 1990, and third amended disclosure statement on December 20, 1990. The bankruptcy court approved the third amended disclosure statement following a hearing on December 21, 1990.

Beginning January 23, 1991, and continuing on four additional days, the bankruptcy court conducted a hearing to determine whether debtor's fourth amended plan should be confirmed. Before taking up the matter of plan confirmation, the bankruptcy court heard and considered various pending motions. First, the court considered and granted debtor's applications to approve the employment of an appraiser and an architect, nunc pro tunc. The court then considered and denied Heartland's motions for administrative claim and for deposit of consideration. During the confirmation hearing, the bankruptcy court heard the testimony of Anne Sadovsky, debtor's marketing agent, and approved debtor's application to employ her, nunc pro tunc. At the conclusion of the confirmation

hearing on March 14, 1991, the bankruptcy court stated that the prospect of debtor's meeting the debt service requirement of the plan was "marginal." Nevertheless, on April 23, 1991, the bankruptcy court signed its findings of fact and conclusions of law and rendered its order confirming debtor's fourth amended plan of reorganization.[1]

Heartland filed separate appeals from the bankruptcy court's orders (1) confirming debtor's fourth amended plan of reorganization, (2) employing and retaining James W. Daniels & Associates, Inc., as appraiser, (3) denying motion to allow administrative claim, (4) employing and retaining John R. Horton, Inc., as architectural design and supervision company, and (5) denying Heartland's motion for deposit of consideration.

Apparently the bankruptcy court did not sign a separate order approving the application to employ marketing agent, nunc pro tunc, as it had on the applications to approve employment of an appraiser and an architect. The docket sheet reflects, and the record on appeal contains, only a proceeding memorandum noting that the application was granted. Presumably, for that reason Heartland did not file a separate appeal as it did with regard to the other applications and motions heard at the confirmation hearing. In any event, Heartland did include the approval of the marketing agent's employment as an issue on appeal of the plan confirmation and debtor has not complained of the procedure followed.

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[1]A copy of the bankruptcy court's findings of fact and conclusions of law taken from the record is attached as an appendix to this memorandum opinion and order.

IV.
The Plan

Debtor's plan is typical of Chapter 11 reorganization plans in that it begins with a list of definitions of terms used in the plan (Article I), certain general terms and conditions (Article II), and the classification of claims and interests (Article II). Article IV describes the treatment of the six classes of claims, to wit:

Class 1 allowed administrative claims;
Class 2 allowed priority claims;
Class 3 allowed City claim;
Class 4 allowed Heartland claim;
Class 5 allowed unsecured claims; and
Class 6 holders of interests in the debtor.

In particular, it provides that City's claim is to receive the same treatment as the Class 5 unsecured claims. Holders of Class 5 claims are to receive a pro rata share of the beneficial interests in the Regalridge trust, hereinafter described, evidenced by certificates of beneficial interest. The Regalridge trustees are to make periodic cash payments on at least an annual basis when they, in their discretion, determine that the trust has available net cash flow that is not required to be reserved for another purpose.

As for Heartland's claim, the plan provides that the secured portion thereof shall be paid in monthly installments of principal and interest as though amortized over thirty years from the effective date of the plan, with interest at the rate provided in the January 31, 1984, promissory note executed by debtor. The secured claim is

to be paid in full upon the sale of the property or the expiration of fifteen years, whichever shall first occur. If Heartland fails to make a timely § 1111(b) election, the unsecured portion of its claim is to receive the same treatment as Class 5 unsecured claims. Article IV further provides that Heartland will retain its lien in the property and that

> all other terms and conditions of the treatment of [Heartland's claim] described in the plan and the lien securing same shall be similar to the original terms of Heartland's note and lien, except where inconsistent with the letter and spirit of this plan.

Fourth Amended Plan of Reorganization at 12, ¶ 4.4.c. The plan does not contain as an exhibit or otherwise the note and deed of trust, or any of the terms thereof, to be executed in favor of Heartland.

Articles V and VI describe plan implementation and formation of the Regalridge trust, to which ownership of the property is to be transferred. The trust is to be governed by three trustees to be selected, one each, by the Fort Worth NAACP, City, and Heartland. The Fort Worth NAACP is not a creditor of debtor. The plan provides that the trustees will have exclusive power and control over the operation of Regalridge and that they will not be subject to any court supervision.

Articles VII through XIV contain the remaining plan provisions. None of these is particularly pertinent to the issues raised on appeal, except that paragraph 8.2 of Article VIII does provide that the plan may be modified

following confirmation after notice and hearing.

V.
Issues on Appeal

Heartland asserts fifty-one issues on appeal, many of which appear to present different shades of the same matter. Heartland's issues are:

1. Whether the Bankruptcy Court erred in confirming the Debtor's Fourth Amended Plan of Reorganization.

2. Whether the Bankruptcy Court erred in finding that the Debtor's Plan complied with each and every one of the requirements for confirmation under § 1129(a)(1)-(11) and § 1123 of the Bankruptcy Code.

3. Whether the Bankruptcy Court erred in finding and concluding that the Debtor had met its burden of proof on the requirements of §1129(a) and §1123 by the preponderance of the evidence.

4. Whether the Bankruptcy Court erred in finding that the debtor's Plan met each of the requirements for confirmation under § 1129(b).

5. Whether the Bankruptcy Court erred in finding that the Debtor had met its burden of proof on the requirements of § 1129(b) by clear and convincing evidence.

6. Whether the Bankruptcy Court erred in approving the applications to employ professionals nunc pro tunc.

7. Whether the Bankruptcy Court erred in approving the payments made to professionals.

8. Whether the Bankruptcy Court was clearly erroneous in its findings.

9. Whether the Bankruptcy Court erred in entering the following orders on January 25, 1991: (a) Order Employing and Retaining John R. Horton, Inc. as Architectural Design and Supervision Company; (b) Order Employing and Retaining James W. Daniels and Associates as Appraiser for the Debtor; and (c) Order Denying Heartland's Motion for Deposit of Consideration to be Distributed Under Plan.

10. Whether the Bankruptcy Court erred in entering an Order Denying Heartland's Motion to Allow Administrative Claim on January 24, 1991.

11. Whether the Bankruptcy Court erred in entering the Order Confirming the Debtor's Fourth Amended Plan of Reorganization ("Plan") on April 24, 1991.

12. Whether the Bankruptcy Court erred in approving the Debtor's Third Amended Disclosure Statement on December 21, 1990, and in finding that the Debtor's Third Amended Disclosure Statement contained adequate information as required by 11 U.S.C. §1125.

13. Whether the Bankruptcy Court erred in finding that the Debtor's modifications to the Plan, which were included in the Plan after voting thereon, did not adversely change the treatment of the claim of any creditor.

14. Whether the Bankruptcy Court erred in finding that (a) a reasonable basis exists for separate classifications of the claims and interests in each class, (b) that the claims and interest of each class under the Plan are substantially similar under the Plan and (c) such classification satisfies the requirements of §1122(a) of the Bankruptcy Code.

15. Whether the Bankruptcy Court erred in finding that the interest holders and the Debtor do not receive or retain any property under or pursuant to the Plan.

16. Whether the Bankruptcy Court erred in finding that Heartland was required to make an election under § 1111(b) in order to have its secured claim classified separately from its unsecured claim.

17. Whether the Bankruptcy Court erred in finding that two unsecured classes of non-insider creditors voted to accept the Plan.

18. Whether the Bankruptcy Court erred in finding that ". . . the control of two classes by Heartland effectuates a non-substantive and technical amendment to the Plan." Record No. 152, Findings p. 4, ¶ 15.

19. Whether the Bankruptcy Court erred in overruling Heartland's objections to confirmation of the Plan based on technical issues relating to classification.

20. Whether the Bankruptcy Court erred in finding that the provisions of the Plan regarding the procedure for selection, appointment, removal, qualifications and duties of the "Regalridge Trustees" and

who was to select these trustees are consistent with the interests of creditors and with public policy.

21. Whether the Bankruptcy Court erred in finding that the Plan provides for distribution to creditors on a pro-rata basis of the cash flow on at least an annual basis.

22. Whether the Bankruptcy Court erred in finding that (1) Heartland will retain its liens under the Plan, (2) the property will probably support debt service equal to Heartland's secured claim, and (3) Heartland will receive the present value of its secured claim.

23. Whether the Bankruptcy Court erred in finding that, ". . . over the next six years, money will be available as cash flow for distribution to creditors whose claims will be treated as unsecured Class 5 claims after payment of ordinary and necessary operating expenses and payment of debt service on Heartland's secured claim." Record No. 152, Findings p. 7, ¶ 27.

24. Whether the Bankruptcy Court erred in finding that Heartland's unsecured deficiency claim is in the approximate amount of $10,000,000.00.

25. Whether the Bankruptcy Court erred in finding that the Class 5 creditors accepted the Plan and that no Class 5 creditors voted against the Plan.

26. Whether the Bankruptcy Court erred in finding that the Plan is feasible.

27. Whether the Bankruptcy Court erred in finding that the Plan has even a marginal prospect of

success. Record No. 152, Findings p. 7, ¶ 31.

28. Whether the Bankruptcy Court erred by failing to apply the correct legal standard in confirming the Plan.

29. Whether the Bankruptcy Court erred in accepting the Debtor's projections while cautioning that the Debtor ". . . will have to work diligently to make the Plan succeed." Record No. 152, Findings, p. 7, ¶ 36.

30. Whether the Bankruptcy Court erred in finding that only $250,000.00 to $300,000.00 is needed to make repairs on the property.

31. Whether the Bankruptcy Court erred in finding that the value of the property and Heartland's secured claim is $8,200,000.00.

32. Whether the Bankruptcy Court erred by applying an improper legal standard to determine the value of Heartland's collateral and secured claim.

33. Whether the Bankruptcy Court erred in finding that the property will generate sufficient cash flow to pay necessary and normal operating expenses, the secured debt of Heartland at a market rate of interest, and a dividend to Class 5 creditors.

34. Whether the Bankruptcy Court erred in finding that for the past several months the Debtor has met or exceeded $200,000.00 per month in income and that an income of $200,000.00 per month will be sufficient to fund the Plan.

35. Whether the Bankruptcy Court erred in finding that occupancy at the property has increased from 55% to 85% and will probably increase to 90% in the first half of 1991.

36. Whether the Bankruptcy Court erred in finding that (a) the Debtor has demonstrated an ability to make needed repairs on the property, (b) some needed repairs to the property could be delayed until the end of the year and, (c) cash flow will be available by the end of the year to pay for deferred repairs.

37. Whether the Bankruptcy Court erred in finding that the Plan is not likely to be followed by the need for further financial reorganization or liquidation.

38. Whether the Bankruptcy Court erred in finding that, notwithstanding Heartland's rejection of the Plan, the Plan may be confirmed pursuant to §1129(b), that the Plan does not discriminate unfairly against and is fair and equitable to Heartland.

39. Whether the Bankruptcy Court erred in finding that the treatment of Heartland's deficiency claim in Class 5 is identical to the treatment of all Class 5 claims.

40. Whether the Bankruptcy Court erred in finding that the Plan protects the legal rights of Heartland's unsecured deficiency claim.

41. Whether the Bankruptcy Court erred in finding that ". . . no holder of any claim or interest junior to Heartland's claims under the Plan will receive or retain on account of the junior claim or interest any property under the Plan". Record No. 152, Findings p. 10, ¶ 43.

42. Whether the Bankruptcy Court erred in denying Heartland's Motion to Dismiss or Convert the bankruptcy case.

43. Whether the Bankruptcy Court erred in its failure to make any finding regarding the apparent grant of a discharge of the interest holders of the Debtor.

44. Whether the Bankruptcy Court erred in its failure to make any finding regarding the establishment and use of the Distribution Fund.

45. Whether the Bankruptcy Court erred in its failure to make a finding that the projections used by the Debtor at the Confirmation hearing were not the same projections mailed out to the creditors for voting on the Plan.

46. Whether the Bankruptcy Court erred in its failure to make a finding that the change in projections was a material change to the Plan.

47. Whether the Bankruptcy Court erred in its failure to make any findings regarding the fairness, specificity or legality of any of the provisions of the Regalridge Trust Agreement and Plan.

48. Whether the Bankruptcy Court erred in relying upon the Court's personal observations of the property in confirming the Plan.

49. Whether the Bankruptcy Court erred in denying Heartland's Motion to Strike Affidavit of Tallying Agent.

50. Whether the Bankruptcy Court erred in finding that the balloting of classification of creditors was proper and that any error in the balloting of classification of any creditors was harmless.

51. Whether the Bankruptcy Court erred in entering an Order Approving and Granting Amendment to the Confirmed Fourth Amended Plan of Reorganization.

Having thus listed the issues, Heartland proceeds to divide its brief into categories as follows:

I. The debtor's plan is not feasible, § 1129(a)(11).

II. The plan fails to meet the mandatory requirements for confirmation under the Bankruptcy Code.

III. The plan fails to meet the requirements for cramdown under the Bankruptcy Code, § 1129(b).

IV. The plan violates the absolute priority rule.

V. The plan fails to comply with the mandatory provisions of § 1123.

VI. The plan expends Heartland's cash collateral for unallowable purposes, § 506(c).

VII. Improper approval of professionals and their fees, nunc pro tunc.

VIII. Heartland's administrative claim and motion for deposit of consideration.

Heartland does not state which particular issues belong to each of these categories.

The court's discussion of the issues will focus on the eight categories defined by Heartland, but will be organized in what seems to the court to be a more logical order. The court considers that any of the issues on appeal not specifically discussed and supported by Heartland in the body of its briefs is waived. McGrudser v. Necaise, 733 F.2d 1146, 1148 (5th Cir. 1984); Ronit, Inc. v. Block Shim Development Co. - Irving In re Block Shim Development Co. - Irving), 118 B.R. 450, 452 n.2 (N.D. Tex. 1990), aff'd, 939 F.2d 289 (5th Cir. 1991).

VI.
Standard of Review

To the extent the appeal presents questions of law, the bankruptcy court's judgment is subject to de novo review. Pierson & Gaylen v. Creel & Atwood (In re Consolidated Bancshares, Inc.), 785 F. 2d 1249, 1252 (5th Cir. 1986). Findings of fact, however, will not be set aside unless clearly erroneous. Memphis-Shelby County Airport Authority v. Braniff Airways, Inc. (In re Braniff Airways, Inc.), 783 F.2d 1283, 1287 (5th Cir. 1986). A finding is clearly erroneous, although there is evidence to support it, when the reviewing court on the entire evidence is left with a definite and firm conviction that a mistake has been committed. Id. The mere fact that this court would have weighed the evidence differently if sitting as the trier of fact is not sufficient to set aside the bankruptcy court's order if that court's account of the evidence is plausible in light of the record viewed in its entirety. Anderson v. City of Bessemer City, 470 U.S. 564, 573-74 (1985).

Although the parties doubtless would agree with the foregoing recitation of the standard of review on appeal, they disagree as to the burden of proof on debtor at the confirmation hearing. Heartland maintains that debtor had to prove the confirmability of its plan by clear and convincing evidence.[2] Debtor, on the other hand, states that the preponderance of the evidence[3] standard applies in all bankruptcy matters, relying on Grogan v. Garner, 111 S. Ct. 654 (1991).

In Grogan, the United States Supreme Court determined that the preponderance of the evidence standard is the appropriate standard of proof for the dischargeability exceptions in 11 U.S.C. § 523(a). 111 S. Ct. at 661. Following Grogan, the Tenth Circuit determined that the preponderance of the evidence standard also applies to dischargeability under 11 U.S.C. § 727. First National Bank of Gordon v. Serafini (In re Serafini), 938 F.2d 1156, 1157 (10th Cir. 1991). Both of these cases recognize that a debtor has no constitutional or fundamental right to a discharge that would entitle him

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[2]Evidence is clear and convincing if it places in the factfinder an abiding conviction that the truth of the factual contentions is highly probable. Colorado v. New Mexico, 467 U.S. 310, 316 (1984); Kaszuk v. Bakery & Confectionary Union, 638 F.Supp. 365, 374 (N.D. Ill. 1985), aff'd, 791 F.2d 548 (7th Cir. 1986).

[3]A preponderance of the evidence means proof sufficient to persuade the finder of fact that the proposition is more likely true than not true. Hopkins v. Price Waterhouse, 737 F. Supp. 1202, 1206 (D.D.C.), aff'd, 920 F.2d 967 (D.C. Cir. 1990).

to a heightened standard of proof. Grogan, 111 S. Ct. at 659; Serafini, 938 F.2d at 1157 n.2. The holdings in both cases are limited to the issue of dischargeability.

The court is not convinced that Grogan was intended to accomplish a wholesale destruction of the precedents set with regard to the debtor's burden of proof in other bankruptcy contexts. Grogan speaks only to the creditor's, not the debtor's, burden of proof with regard to dischargeability. The debtor's burden has traditionally been one of clear and convincing evidence, at least in the context of a cramdown. See In re Murel Holding Corp., 75 F.2d 941, 942 (2nd Cir. 1935); B.W. Alpha, Inc. v. First City Nat'l Bank of San Angelo, N.A. (In re B.W. Alpha, Inc.), 100 B.R. 831, 833 (N.D. Tex. 1988); In re Future Energy Corp., 83 B.R. 470, 481 (Bankr. S.D. Ohio 1988). Some courts have indicated that the same standard applies under 11 U.S.C. § 1129(a). In re Rusty Jones, Inc., 110 B.R. 362, 373 (Bankr. N.D. Ill. 1990); In re Agawam Creative Marketing Assocs., Inc., 63 B.R. 612, 619 (Bankr. D. Mass. 1986). The clear and convincing test is the logical one to apply because of the stricter scrutiny required when property and property rights are sought to be taken. Cf. Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555 (1935) (recognizing the substantive rights of a secured creditor in specific property and noting that the bankruptcy power is subject to the Fifth Amendment). There is no question that debtor has failed to meet this burden of proof. Moreover, even if the court's analysis is incorrect and the appropriate burden of proof is one of preponderance of the evidence, the result would be the same.

VII.
Confirmability of Debtor's Plan

A. Feasibility

To be confirmed, a debtor's plan of reorganization must be feasible. 11 U.S.C. § 1129(a)(11); In re N.S. Garrott & Sons, 48 B.R. 13, 15 (Bankr. E.D. Ark. 1984). The burden of proving feasibility belongs to the debtor. In re Lakeside Global II, Ltd., 116 B.R. 499, 505 (Bankr. S.D. Tex 1989). To demonstrate feasibility, the debtor must show by concrete evidence that there will be sufficient cash flow to fund the plan and maintain operations according to the plan. In re Nelson, 84 B.R. 90, 93 (Bankr. W. D. Tex. 1988); In re Merrimack Valley Oil Co., 32 B.R. 485, 488 (Bankr. D. Mass. 1983). Factors to be considered include the debtor's prior performance, the adequacy of capital structure, the earning power of the business, economic conditions, the ability of management, the probability of the continuance of the same management, and any other related matter that determines the prospects of a sufficiently successful operation to enable performance of the provisions of the plan. Canal Place Limited Partnership v. Aetna Life Ins. Co. (In re Canal Place Limited Partnership), 921 F.2d 569, 579 (5th Cir. 1991) (per curiam approving bankruptcy court's analysis set forth as appendix to the opinion); Lakeside Global, 116 B.R. at 506. Plans that are mere visionary schemes based on speculation, conjecture, or unrealistic projections cannot be confirmed. In re Sound Radio, Inc., 93 B.R. 849, 856 (Bankr. D.N.J. 1988), aff'd in part, remanded in part, 103 B.R. 521 (D.N.J. 1989), aff'd, 908 F.2d 964 (3rd Cir. 1990).

Here, Heartland maintains that debtor's plan is but a visionary scheme because debtor has not been able to meet its own operating projections in the past and its expectations for future performance are unsupported. For example, in April 1990, debtor submitted a budget in connection with its opposition to Heartland's motion to lift the automatic stay, which projected expenditures of $1,115,000.00 for 1990. Debtor's actual expenditures for 1990 were $1,807,000.00 — thirty-eight percent more than anticipated. As for the future, debtor projects, and its plan's success depends upon achievement of, a ninety percent economic occupancy rate for 1991. Debtor has never before been able to achieve more than an eighty-five percent physical occupancy rate, at which time the economic occupancy rate was only sixty-eight and 08/100 percent. Even debtor's own expert projected a seventy percent economic occupancy rate for 1991.

More important than past inability to meet expectations is the lack of evidence to support present ability to make a plan work. Debtor's plan provides that Heartland is to receive, over a period of fifteen years, installments of interest plus only twenty percent of the principal of its secured debt. At the end of fifteen years, debtor will make a balloon payment to Heartland of approximately $6,500,000. It appears that virtually all of the income generated from Regalridge will be required to fund the plan and to keep Regalridge operating. Debtor has not made any showing of how it will be able to make the balloon payment to Heartland at the end of fifteen years. Because the plan calls for debtor to be operating on a shoestring and there has been no showing of the source of funds for the balloon payment, it is difficult to see how the plan could be feasible under the Code. Lakeside Global, 116 B.R. at 507.

In response debtor points to other evidence reflecting improved conditions at Regalridge and urges the court that two different interpretations can be made from the same set of facts. That being the case, debtor urges that the court must defer to the bankruptcy court's findings. Amadeo v. Zant, 486 U.S. 214, 223 (1988). In order for deference to be mandated, however, the bankruptcy court's findings must be plausible in light of the record viewed in its entirety. Anderson, 470 U.S. at 574. Here, the record as a whole reflects the uncertainty inherent in debtor's plan. Debtor offered no evidence on the future value of the property or on the source of funds for the balloon payment. Debtor recognizes that ninety percent economic occupancy is necessary in order for the plan to be funded, yet admits that ninety percent economic occupancy has never before been achieved.[4]

In sum, "feasibility" means that confirmation of a plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or

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[4]Debtor further argues that the plan is somehow made more feasible by the voiding of appellant's lien in debtor's personalty. See March 25, 1991, order signed by Judge Mahon in CA4-90-818-E. The lien avoidance occurred subsequent to the confirmation hearings and is not an issue on appeal. The record reflects that personalty was not included in the valuations of the property before the bankruptcy court. This point is now moot in any event, however, as the Fifth Circuit has reversed the district court's order and affirmed the decision of the bankruptcy judge denying avoidance of appellant's lien. See Heartland Federal Savings & Loan Ass'n v. Briscoe Enterprises, Ltd., II, No. 91-1525 (5th Cir. Feb. 14, 1992).

any successor to the debtor under the plan. 11 U.S.C. § 1129(a)(11). A plan that has a "marginal prospect of success"[5] because the debtor's "prospects of meeting the debt service required"[6] under the plan of reorganization are marginal is not, as a matter of law, a feasible plan. Therefore, the bankruptcy court's findings and conclusions set forth in item Nos. 31, 36, 37 and 38 of the April 24, 1991, findings of fact and conclusions of law [hereinafter "Findings"] must be set aside.[7]

B. Other Requirements of 11 U.S.C. § 1129(a)

In addition to being feasible, a plan must meet a number of other requirements, including those set forth at 11 U.S.C. §§ 1129(a)(1)-(4), (7) and (8). These requirements are briefly that: the plan comply with applicable provisions of the Bankruptcy Code [§ 1129(a)(1)]; debtor comply with applicable provisions of the Bankruptcy Code [§ 1129(a)(2)]; the plan be proposed in good faith [§ 1129(a)(3)]; payments made or to be made be approved by the bankruptcy court [§ 1129(a)(4)]; the plan meet the best interest test [§ 1129(a)(7)]; and, each impaired class must accept the plan [§ 1129(a)(8)]. Heartland claims that these requirements have not been met. A brief discussion follows with regard to each of them, except § 1129(a)(8). There is no question that each impaired class has not accepted the plan and that the plan

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[5]Findings of Fact and Conclusions of Law No. 31.

[6]Tr. Vol. V at 72.

[7]The bankruptcy court's determination, set forth in item 35, that the value of Heartland's secured claim is $8.2 million dollars is discussed infra.

is subject to the cramdown provisions of § 1129(b). See Findings No. 28.

1. Compliance with Applicable Code Provisions

Heartland argues that the plan fails to comply with § 1129(a)(1), because the plan is not feasible[8] and because the requirements of §§ 1123, 506(c), and 1125 have been violated. Heartland further asserts that the plan improperly classifies claims in an attempt to divest Heartland of the right to cast a vote based on its unsecured claim.[9] Heartland also maintains that debtor itself has failed to comply with applicable provisions of the Bankruptcy Code, in violation of 11 U.S.C. § 1129(a)(2).

Section 1123 sets forth the requirements for items to be included in reorganization plans. Pursuant to § 1123(a)(2), a plan must specify any class of claims or interests that is not impaired under the plan. In re Polytherm Indus., Inc., 33 B.R. 823, 829 (W.D. Wis. 1983). Although the better practice is to include a statement of whether each class of claims is impaired or unimpaired, all that is required is that there be a basis upon which a creditor can determine whether a class of claims is impaired. In re AG Consultants Grain Div., Inc., 77 B.R. 665, 670 (Bankr. N.D. Ind. 1987). In this case, one can easily determine from the plan which claims are

[8]See discussion of feasibility at pp. 17-20, supra.

[9]Although Heartland's opening brief devotes only one sentence to this issue, debtor's brief and Heartland's reply thereto discuss the issue at some length. Accordingly, the court considers that the issue is properly preserved.

unimpaired.

Section 1123(a)(3) requires that a plan specify the treatment of any class of claims that is impaired under the plan. This section means that if a plan provides for future cash payments, it must set forth the dollar amount of each payment and the date upon which it will be made. Sandy Ridge Dev. Corp. v. Louisiana Nat'l Bank (In re Sandy Ridge Dev. Corp.), 881 F.2d 1346, 1353 (5th Cir. 1989). The plan in this case does not contain the requisite specificity as to payments to be made.[10] Nor does the plan specify the terms of the note and deed of trust to be retained by Heartland.[11]

Section 1123(a)(4) requires that the plan provide the same treatment to each claim or interest of a particular class unless the holder of a particular claim agrees to less favorable treatment. Heartland complains that until January 22, 1991, the city was the only unsecured

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[10]For example, the plan provides that creditors will receive periodic cash payments at the discretion of the Regalridge trustees "but only to the extent that such payments do not effect the normal operations of the Property." Fourth Amended Plan of Reorganization at ¶ 6.2. In other words, creditors may or may not receive any such payments.

[11]Findings No. 16 addresses § 1123(a)(3), but states only that "Article 4 of the Plan describes the treatment to be afforded to each of the impaired classes." To the extent that this statement implies that the requirements of § 1123(a)(3) have been met, it is erroneous and must be set aside.

creditor entitled to select one of the three Regalridge trustees. The fact is, however, that the plan was amended to allow Heartland to select a trustee as well. No other unsecured claimants have complained of less favorable treatment and Heartland does not have standing to assert a complaint on their behalf in this regard. In re Orlando Investors, L.P., 103 B.R. 593, 597 (Bankr. E.D. Pa. 1989).

Section 1123(a)(5) requires that the plan provide adequate means for its implementation. This means that the debtor must offer more than speculation about the source of funding for the plan. In re Stuart Motel, Inc., 8 B.R. 48, 50 (Bankr. S.D. Fla. 1980). As previously discussed, debtor failed to provide information about its ability to refinance the property or sell it at a later date for a particular price. Debtor also failed to provide the note and deed of trust to be retained by Heartland. More importantly, debtor failed to show how the plan would be funded absent ninety percent economic occupancy, which had never before been achieved. For these reasons, the plan does not meet the requirements of § 1123(a)(5) and Findings No. 17 will be set aside.

Section 1123(a)(7) requires that the plan contain only provisions consistent with public policy and the interests of creditors and equity security holders regarding the manner of selection of any officer, director or trustee or their successors under the plan. Heartland complains because the plan calls for the selection of a trustee by the NAACP, which is not a creditor of debtor. The record reflects, however, that the NAACP has an interest in maintaining and preserving Regalridge. Heartland fails to show how the plan is inconsistent with, or adverse to, the interests of the public.

Heartland next complains that its cash collateral, that is, rents from the property, has been and will continue to be used to pay administrative expenses including professional fees incurred by debtor. Although cash collateral, e.g. rental income, may be used to pay ordinary and necessary operating expenses, it may not be used to pay administrative expenses or general costs of reorganization, except under extraordinary circumstances. French Market Homestead, F.S.A. v. P.C., Ltd. (In re P.C., Ltd.), 929 F.2d 203, 205 (5th Cir. 1991); New Orleans Pub. Serv., Inc. v. First Fed. Sav. & Loan Ass'n (In re Delta Towers Ltd.), 924 F.2d 74, 76 (5th Cir. 1991); In re Tripplet, 84 B.R. 84. 87 (Bankr. W.D. Tex. 1988). The exception is set forth in 11 U.S.C. § 506(c) and provides that the debtor must show that: (1) the expenditure is necessary; (2) the cost is reasonable; and (3) the expenses were incurred primarily for the benefit of the secured creditor and resulted in a quantifiable direct benefit to that creditor. In re P.C., Ltd., 929 F.2d at 205; General Elec. Credit Corp. v. Levin & Weintraub (In re Flaggstaff Foodservice Corp.), 739 F.2d 73, 75 (2nd Cir. 1984). The claim of an attorney rendering services to an estate is not entitled to priority over the claim of a secured creditor to its collateral. In re A.J. Lane & Co., 113 B.R. 821, 824 (Bankr. D. Mass. 1990). Therefore, to the extent the plan calls for the payment of debtor's attorney's fees or any other professional fees or extraordinary expenses out of Heartland's cash collateral, the plan violates § 506 (c).

Heartland additionally complains that the plan was improperly solicited, in violation of 11 U.S.C. § 1125, because debtor did not mail to creditors for their review a revised budgeted cash flow statement. Heartland maintains that the revised statement (Heartland's Exhibit 98) "substantially increased the expense projections beyond

what was described in the [third amended disclosure statement]" (Heartland's Exhibit 63). Heartland's Brief at 31. Heartland fails to mention that the revised statement also reflects a greater amount available for debt service. As debtor points out, a bankruptcy court may permit testimony at trial that varies from the information included in its disclosure statement, especially where that evidence indicates even stronger prospects for successful reorganization. Prudential Ins. Co. v. Monnier (In re Monnier Bros.), 755 F.2d 1336, 1342 (8th Cir. 1985).

Finally, on the subject of the plan's failure to comply with code provisions, Heartland complains that its unsecured claim, the City's unsecured claim, and the unsecured claims of debtor's trade creditors were improperly placed in separate classes in "an attempt to divest Heartland of its substantive right to cast a vote for its unsecured claim." Heartland Brief at 30-31. By placing the unsecured claims in separate classes, debtor made certain that at least one impaired class would vote to accept the plan, making a cramdown possible. See 11 U.S.C. § 1129(a)(10). Debtor attempts to justify its separate classification of the City's unsecured claim by noting that the claim was originally secured and now is not. Debtor does not offer, nor has the court found, any support for this position. Debtor additionally argues that its classification, if erroneous, constituted only a technical impropriety because all unsecured claims are treated the same way under the plan. The rule in the Fifth Circuit, however, is that substantially similarly claims should be placed in the same class and, further, that similar claims cannot be classified differently in order to gerrymander an affirmative vote on a reorganization plan. Phoenix Mutual Life Ins. Co. v. Greystone III Joint Venture (In re Greystone III Joint Venture), 948 F.2d 134, 139 (5th Cir.

1992). As in Greystone, there is no support in the record for the bankruptcy court's conclusion that a reasonable basis exists for separate classifications of the unsecured claims. Thus, Findings Nos. 13 and 15 must be set aside.

Heartland also argues that debtor itself has failed to comply with the applicable Bankruptcy Code provisions, as evidenced by debtor's employment of, and payments to, professionals without prior court approval. Debtor replies that its later filing of motions for authorizations nunc pro tunc, which were approved, vitiates its earlier noncompliance with the Code. If that were all that was required, there would be no need for § 1129(a)(2).[12]

2. Good Faith

Heartland maintains that the plan was not proposed in good faith because there is not a reasonable likelihood that the plan will achieve a result consistent with the purposes and objectives of the Bankruptcy Code, i.e., the plan does not provide for expeditious resolution of disputes and speedy payment to creditors. See In re Madison Hotel Assoc., 749 F.2d 410, 424 (7th Cir. 1984); In re Hoosier Hi-Reach, Inc., 64 B.R. 34, 38 (Bankr. S.D. Ind. 1986). Whether a plan is proposed in good faith must be determined in light of the circumstances surrounding the plan. In re Texas Extrusion Corp., 844 F.2d 1142, 1160 (5th Cir.), cert. denied, 488 U.S. 926 (1988). In other words, objective, rather than subjective, intent of the debtor determines whether a plan is proposed in good faith.

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[12]The bankruptcy court did not make a specific finding or state a conclusion with regard to § 1129(a)(2).

The record does not support a finding of objective good faith, because the plan is not feasible. Moreover, despite the debtor's enthusiasm and the public's interest in maintaining Regalridge as a going concern, debtor's actions during the pendency of the bankruptcy call into question its subjective good faith. For example, debtor violated the bankruptcy court's order regarding the use of rents by knowingly making payments to professionals without prior court approval. Further, at the last minute, debtor filed a motion for approval of amendment to its fourth amended plan of reorganization, which amendment sought to change crucial definitions in the plan so as to enable debtor to consummate its plan pending Heartland's appeal to this court.[13] Accordingly, Findings No. 22 will be set aside.

3. Approval of Fees and Expenses

Next, Heartland complains that the plan calls for the payment of all fees and expenses to be within the discretion of the Regalridge trustees, who are not subject to court supervision. As debtor correctly notes, however, upon plan confirmation, a debtor is no longer a debtor in possession and the bankruptcy estate ceases to exist. In re NTG Indus., Inc., 118 B.R. 606, 610 (Bankr. N.D. Ill. 1990). In other words, the reorganized debtor is a new entity not subject to the jurisdiction of the bankruptcy

[13]Heartland notes that the motion was granted less than twenty-four hours after its filing. The record does not reflect whether debtor played any active role in presenting the motion for signature without notice to Heartland. The court has not considered the quick approval of the motion as any evidence with regard to debtor's good faith or lack thereof.

court, except as provided in the plan. Therefore, approval of fees for post-confirmation services is not required. Moreover, although 11 U.S.C. § 1129(a)(4) calls for approval of fees for preconfirmation services, Heartland does not contend that the fees for any such services have not been disclosed or that approval for payment of same will not be sought. The plan need not contain a specific provision mandating that all relevant payments be subject to court approval. In re Future Energy Corp., 83 B.R. 470, 488 (Bankr. S.D. Ohio 1988).

4. Best Interest Test

Heartland claims that the plan fails to meet the best interest test, which requires that a dissenting creditor must receive on account of his claim property of a value, as of the effective date of the plan, that is not less than the amount the creditor would receive under a Chapter 7 liquidation. In re Elm Creek Joint Venture, 93 B.R. 105, 109 (Bankr. W.D. Tex. 1988). Debtor responds that Heartland will receive more on its unsecured claim under the plan than in a liquidation,[14] but the record does not support this contention. As previously stated, debtor made no showing that the property could or would be later sold for an amount sufficient to pay off Heartland's secured claim or to whom such sale would be made. Moreover, because the plan does not set forth the terms of the new

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[14]Debtor further states, echoing the bankruptcy court's statements in item 27 of the Findings, that all unsecured creditors are better off under the plan. The test, however, is not how the plan affects creditors in general, but rather whether the dissenting creditor will receive not less than the amount he would receive under Chapter 7 liquidation.

deed of trust to be executed in favor of Heartland, there is no assurance that Heartland's rights as a secured creditor will not be altered. Findings Nos. 26 and 27 must be set aside.

C. Whether the Plan Meets the Requirements for Cramdown

1. Fairness and Equity

To be confirmed over the objection of an impaired secured creditor, a plan of reorganization must not discriminate unfairly and must be fair and equitable with respect to the secured claim. 11 U.S.C. § 1129(b). "Fair and equitable" as used in the context of a cramdown means that, at a minimum, the secured creditor must receive the indubitable equivalent of his secured claim. In re Sandy Ridge Dev. Corp., 881 F.2d at 1349-50. In other words, mere technical compliance with § 1129(b)(2) does not assure that the reorganization plan is fair and equitable. Federal Sav. & Loan Ins. Corp. v. D&F Constr., Inc. (In re D&F Constr., Inc.), 865 F.2d 673, 675 (5th Cir. 1989). Rather, the court must consider the plan as a whole and all of the facts and circumstances surrounding treatment of the creditor's claim. Id.

The concept of indubitable equivalence was enunciated by Judge Learned Hand in In re Murel Holding Corp.:

> It is plain that "adequate protection" must be completely compensatory; and that payment ten years hence is not generally the equivalent of payment now. Interest is indeed the common measure of the

> difference, but a creditor who fears the safety of his principal will scarcely be content with that; he wishes to get his money or at least the property. We see no reason to suppose that the statute was intended to deprive him of that in the interest of junior lienholders, unless by a substitute of the most indubitable equivalence.

75 F.2d 941, 942 (2nd Cir. 1935). The indubitable equivalence standard is stringent. In re Future Energy Corp., 83 B.R. 470, 496. Where a secured creditor receives neither his money nor the property upon which he has a lien, the debtor must show by clear and convincing evidence that the protection provided under the plan to the secured creditor is completely compensatory. In re Murel Holding Corp., 75 F.2d at 942; In re Future Energy Corp., 83 B.R. at 481.

In this case, the record does not support the bankruptcy court's finding that debtor met the strict requirements of § 1129(b)(2). The record does not contain evidence to support debtor's contention that Heartland will be paid in full, e.g. the record does not reflect, because debtor failed to show, what the value of Regalridge will be in fifteen years, that there is any prospect for the sale or refinancing of Regalridge, or who the purchaser or refinancer might be. Moreover, Heartland is not assured that it will retain the liens it now has. Despite debtor's assurance that it intended that the new deed of trust contain the same provisions as the old, no new deed of trust has ever been presented. The plan itself provides that Heartland's secured interest is unaffected except to the extent that it is contrary to the

letter and spirit of the plan, whatever that might mean.

2. The Absolute Priority Rule

The absolute priority rule provides that a dissenting class of unsecured creditors must be compensated in full before any junior class can receive or retain any property under a plan. 11 U.S.C. § 1129(b)(2)(C)(ii); Norwest Bank Worthington v. Ahlers, 485 U.S. 197 (1988); Case v. Los Angeles Lumber Prods. Co., 308 U.S. 106 (1939). Heartland maintains that the plan violates the absolute priority rule because (1) junior creditors will receive payment before Heartland's secured claim is paid in full and (2) its secured claim is not properly valued.

Heartland's first point is well taken. As discussed in the immediately preceding section of this opinion, the record does not reflect that Heartland will receive the indubitable equivalent of its secured claim. In other words, Heartland's claim may not be paid in full. The plan nevertheless calls for payments to junior lienholders before senior claims are paid. The fact that Heartland also has an unsecured claim does not change the requirements of the absolute priority rule.[15]

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[15]In support of its first argument, Heartland additionally points to the fact that debtor selected the persons who would select the Regalridge trustees, and further, the fact that a management company owned by debtor's general partner would qualify to be appointed by the Regalridge trustees to manage Regalridge. Heartland fails to show how either of these facts is relevant. The record does not reflect that debtor will have any control over the Regalridge trustees or that any entity affiliated

As for the issue of valuation of Heartland's secured claim, Heartland fails to explain why such valuation is relevant to the absolute priority rule, which addresses only the treatment of unsecured claims.[16] Relevancy, vel non, Heartland fails to show that the bankruptcy court erred in determining the amount of Heartland's secured claim. The value a secured creditor is entitled to receive and must receive is the value accorded to a buyer in an arm's length transaction, that is, the going concern value of the property. Lakeside Global, 116 B.R. at 513. See also Overholt v. Farm Credit Servs. (In re Overholt), 125 B.R. 202, 215 (S.D. Ohio 1990). Tax liens and the cost of necessary repairs must be subtracted to determine the fair market value of the property, i.e. the allowed secured claim. In re Groff, 131 B.R. 703, 707 (Bankr. E.D. Wis. 1991); Beacon Hill Apartments Ltd. v. Columbia Sav. & Loan Ass'n (In re Beacon Hill Apartments Ltd.), 118 B.R. 148, 149 (N.D. Ga. 1990); Wolk v. Goldome Realty Credit Corp. (In re 222 Liberty Assocs.), 105 B.R. 798, 801 (Bankr. E.D. Pa. 1989).

For the reasons discussed in this section VII, Findings Nos. 41, 42, and 43 must be set aside.

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with debtor will be appointed to manage the property. Heartland further states that the plan provides, and the disclosure statement indicates, that "interest holders" of debtor are to be discharged upon plan confirmation. Heartland's brief at 40. The plain language of the plan and disclosure statement does not support this contention.

[16]Valuation of collateral would seem to be an issue more appropriately addressed in the context of feasibility or fairness and equity.

VIII.
Orders Nunc Pro Tunc

Heartland maintains that the bankruptcy court erred in granting nunc pro tunc debtor's applications for authority to employ an appraiser, an architect, and a marketing consultant. The record reflects that the appraiser was retained by debtor in the summer of 1990 and paid a $4,000.00 retainer; the architect was retained in April 1990 and as of the confirmation hearing had received compensation of almost $25,000.00; the marketing consultant had been retained in August 1990 and had been paid approximately $23,000.00 at the time of the hearing. In December 1990, debtor moved for the retroactive approval of its hiring of these professionals. At the hearing on its applications, debtor admitted that the failure to seek prior approval was "merely an oversight" and something that "fell through the cracks." Tr. Vol. I, 10-12.

The Bankruptcy Code and rules contain specific requirements for the retention and compensation of professionals. See Bankruptcy Code §§ 327 and 330; Bankr. R. 2014 and 2016. Courts in this Circuit require strict adherence to these provisions. See, e.g., In re Consolidated Bancshares, Inc., 785 F.2d at 1254 & n.3. Moreover, nunc pro tunc applications are not to be granted except where there are exceptional circumstances. Fanelli v. Hensley (In re Triangle Chemicals, Inc.), 697 F.2d 1280, 1289 (5th Cir. 1983). Mere oversight in filing a timely application is not an extraordinary circumstance that warrants nunc pro tunc approval. In re Aladdin Petroleum Co., 85 B.R. 738, 739 (Bankr. W.D. Tex. 1988). The bankruptcy court did not find that rare or exceptional circumstances existed nor would the record have supported such a finding. Accordingly, the court finds that the orders

nunc pro tunc approving the employment of professionals must be set aside.

IX.
Denial of Heartland's Administrative Claim

On or about January 3, 1991, Heartland filed its motion to allow administrative claim. The motion recited that, since January 18, 1990, when the bankruptcy court entered an order for use of rents, debtor had paid for all of its operations with Heartland's cash collateral. Heartland alleged that debtor had expended at least $2,193,334.14 as of September 30, 1990, and that Heartland was entitled, pursuant to 11 U.S.C. § 503(b)(1)(A), to recover as an administrative expense that amount plus whatever amounts had been subsequently expended by debtor for preserving and managing the bankruptcy estate.

Debtor filed an objection to the motion, pointing out that Heartland's reading of the Code was absurd and that Heartland was not entitled to an administrative claim except under 11 U.S.C. § 507(b) if its collateral declined in value during the pendency of the bankruptcy. Heartland responded by completely altering its prior position and asserting that it was entitled to an administrative claim for every expense incurred by debtor that debtor could not prove was reasonable and necessary and incurred for Heartland's benefit. The bankruptcy court considered the motion at a hearing on January 23, 1991, and denied the relief sought by order signed January 24, 1991.

Heartland includes among its issues on appeal, almost as an afterthought, that the bankruptcy court erred in denying its motion for administrative claim. Although

none too clear, Heartland's complaint appears to be that debtor was only entitled to use Heartland's cash collateral if debtor could meet the test of 11 U.S.C. § 506(c).[17] Heartland maintains that debtor could not meet the test with regard to its expenditure of at least $284,000.00,[18] and that, therefore, Heartland should have been granted an administrative claim of that amount.

Case law support debtor's, rather than Heartland's interpretation of the Code. In a Chapter 11 case, a debtor in possession has a statutory right to use encumbered assets to operate its business. In re Provincetown-Boston Airline, Inc., 66 B.R. 632, 634 (Bankr. M.D. Fla. 1986). Indeed, most real property reorganizations would fail if the debtor could not use the income stream generated by the property. In re Fry Road Assocs., Ltd., 66 B.R. 602, 604-05 (Bankr. W.D. Tex 1986). The right to use collateral necessary to reorganization may not be taken away unless the secured creditor can demonstrate that it cannot otherwise be adequately protected. In re Provincetown-Boston Airline, Inc., 66 B.R. at 634. In that event, the remedy available to the secured creditor is not through § 503(b), but rather through § 507(b). First State Bank v.

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[17]Appellant further asserts that, "under general principles of subrogation", it "stands in the shoes of those administrative claimants who received its cash collateral." Appellant's brief at 52. The court is unable to comprehend this argument.

[18]The court is unclear as to whether this amount is supported by the record. Appellant cites its own statement of facts in support of this figure, although the amounts recited therein total only $84,971.00.

Advisory Information and Management Systems, Inc. (In re Advisory Information and Management Systems, Inc.), 50 B.R. 627, 629 (Bankr. M.D. Tenn. 1985).

The purpose of § 503(b) is to encourage third parties to provide goods and services necessary for successful reorganization. In re Jartran, Inc., 732 F.2d 584, 588 (7th Cir. 1984). The Code and case law simply do not support any argument that § 503 was intended as an optional remedy to adequate protection provided by § 361. In re Provincetown-Boston Airline, Inc., 66 B.R. at 634. As one court has stated, "the secured creditor is not contributing to the estate by allowing a debtor in possession to use collateral which it already owns and has a statutory right to use." Id.

X.
Deposit of Consideration

The final section of Heartland's appeal brief addresses the bankruptcy court's failure to require the deposit of monies to be distributed upon plan confirmation into a special account. Heartland maintains that the special account is necessary to assure that funds generated from the operation of Regalridge not be used to pay the claims of junior creditors. Heartland asserts that the denial of its motion constituted an abuse of discretion, but cites no authority in support of this proposition. The court is unable to find that the bankruptcy judge abused his discretion in this regard.

XI.
Further Proceedings

There does not appear to be a reasonable likelihood that a confirmable plan could be proposed under the facts of this case. Accordingly, there is no reason why the automatic stay should not be lifted to allow Heartland to foreclose its liens in the property. Further, orders should be made by the bankruptcy court to cause the estate to be reimbursed for any payments it has made to the appraiser, the architectural design and supervision company, and the marketing agent as authorized by the bankruptcy court.

XII.
ORDER

For the reasons set forth herein,

The court ORDERS that:

1. The bankruptcy court's findings of fact and conclusions of law Nos. 12, 13, 15, 17, 22, 26, 27, 31, 36, 37, 38, 41, 42 and 43 be, and are hereby, set aside;

2. The bankruptcy court's orders (a) confirming debtor's fourth amended plan of reorganization, (b) employing and retaining James W. Daniels & Associates, Inc., as appraiser, and (c) employing and retaining John R. Horton, Inc., as architectural design and supervision company, and the ruling of the bankruptcy judge approving the employment of the marketing agent, nunc pro tunc, be, and are hereby, REVERSED; and

The consolidated actions be, and are hereby, remanded for further proceedings consistent with this memorandum opinion and order.

SIGNED April 14, 1992.

s/John McBryde
JOHN MCBRYDE
United States District Judge

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
FORT WORTH DIVISION

In re:	§	
	§	
Briscoe Enterprises, Ltd.	§	Case No.
II, d/b/a Regalridge Square	§	
Apartments,	§	489-44447-MT-11
	§	
Debtor.	§	

ORDER CONFIRMING DEBTOR'S FOURTH AMENDED PLAN OF REORGANIZATION

In conformity with the Findings of Fact and Conclusions of Law entered by this Court in the above styled and numbered bankruptcy proceeding on this date, it is

ORDERED, ADJUDGED AND DECREED that Heartland's Motion to Convert or Dismiss this case be and is hereby DENIED without prejudice.

IT IS FURTHER ORDERED that the Plan proponent's request to confirm the Plan is GRANTED.

IT IS FURTHER ORDERED that the Objection by Heartland and any specific objection not already addressed explicitly or implicitly by the Court's Findings of Fact and Conclusions of Law are OVERRULED.

IT IS FURTHER ORDERED that the Plan be and hereby is CONFIRMED.

IT IS FURTHER ORDERED that all further relief not expressly granted herein be, and it is hereby DENIED.

IT IS SO ORDERED.

SIGNED: April 23, 1991

s/Massie Tillman
Honorable Massie Tillman
United States Bankruptcy Judge

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
FORT WORTH DIVISION

In re:	§	
	§	
Briscoe Enterprises, Ltd.	§	Case No.
II, d/b/a Regalridge Square	§	
Apartments,	§	489-44447-MT-11
	§	
Debtor.	§	

FINDINGS OF FACT AND CONCLUSIONS OF LAW

At Fort Worth, Texas, in said District:

Debtor, Briscoe Enterprises, Ltd., II, d/b/a Regalridge Square Apartments ("Briscoe"), filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code on the 29th day of December, 1989.

On the 23rd day of January, 1991, the Court commenced a hearing on Confirmation of the Debtor's Fourth Amended Plan of Reorganization, continuing on the 24th, 25th and 28th day of January, 1991 and concluding on the 18th day of March, 1991, in the above-styled and numbered bankruptcy case.

Debtor appeared by and through its counsel of record, Weil, Gotshal & Manges. Heartland Federal Savings and Loan ("Heartland"), the only party objecting to confirmation of the Plan of Reorganization, appeared by and through its counsel of record, Gardere & Wynne.

Pursuant to the Court's oral ruling, confirming Debtor's Fourth Amended Plan of Reorganization and after hearing the testimony and evidence presented and reviewing the pleadings, legal memoranda, written arguments of counsel, and legal precedent relevant to the dispute, this Court makes the following additional Findings of fact and Conclusions of Law:

Background

1. On December 29, 1989, Briscoe Enterprises, Ltd. II (the "Debtor") filed a voluntary petition under Chapter 11 of Title 11 of the United States Code (the "Bankruptcy Code").

2. The Debtor's principal asset is a 784-unit low to moderate income property more commonly known as the Regalridge Square Apartments (the "Property"). The Property is located at 4500 Campus Drive, Fort Worth, Texas.

3. Heartland holds an undisputed first lien on the real property comprising the Property pursuant to (a) a Deed of Trust, Assignment of Rents and Security Agreement dated January 31, 1984, which Deed of Trust is recorded in Volume 7731, Page 1534, et. seq. of the Deed of Trust Records of Tarrant County, Texas, and (b) that certain Deed of Trust, Assignment of Rents and Security Agreement dated April 11, 1983, which Deed of Trust is recorded in Volume 7486, Page 2280, et. seq. of the Deed of Trust Records of Tarrant County, Texas. The amount owed to Heartland by the Debtor exceeds the value of the Property. As a result, Heartland is undersecured and holds a substantial unsecured claim against the Debtor. Additionally, because of the value of

the Property and the amounts owed to Heartland, a second lien exceeding $7 million on the Property in favor of the City of Fort Worth also has become a substantial unsecured claim.[1] Because of the lapse of Heartland's UCC-1 Financing Statement, the Debtor has sought to avoid Heartland's lien in and to the personalty, which partially comprises the Property. This Court entered an order denying the Debtor's avoidance action and that issue is currently on appeal to the District Court. The Disposition of that appeal is not relevant to whether the Plan should be confirmed.

4. In June, 1990, Debtor filed its Plan of Reorganization. Thereafter, Debtor's initial bankruptcy counsel was disqualified from further representation of the Debtor in this case. A motion to dismiss or convert this case to a case under Chapter 7 was filed by Heartland. If the case were dismissed or converted, one possible outcome would be Heartland obtaining ownership of the Property through foreclosure.

5. Debtor subsequently retained substitute counsel and thereafter, on November 16, 1990, filed its First Amended Plan of Reorganization, which was later modified by the filing of the Debtor's (a) Second Amended Plan of Reorganization on December 12, 1990, (b) Third Amended Plan of Reorganization on December 20, 1990, and (c) Fourth Amended Plan of Reorganization on January 22, 1991. The Fourth Amended Plan of Reorganization (the "Plan") was the Plan of

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[1]The City of Fort Worth is also the holder of an ad valorem tax claim which is separate and distinct from its $7 million undersecured claim.

Reorganization ultimately presented to the Court for confirmation.

6. On November 16, 1990, the Debtor filed its First Amended Disclosure Statement, which was later modified by the filing of the Debtor's (a) Second Amended Disclosure Statement on December 12, 1990, and (b) Third Amended Disclosure Statement on December 20, 1990. The Third Amended Disclosure Statement (the "Disclosure Statement") was approved by the Court on December 21, 1990, as containing adequate information as required by 11 U.S.C. §1125.

7. The deadline established by the Order for voting on the Plan was January 18, 1991. On January 14, 1991, Heartland filed its objection to the Plan (the "Objection"). No other creditor filed an objection to the Plan. All other creditors and classes allowed to vote on the Plan voted to accept the Plan. Heartland, the Class 4 creditor, voted to reject the Plan, both in its secured and unsecured capacity. The Debtor and Heartland each filed their respective memoranda in support of and in opposition to the Plan.

8. On January 23, 1991, the Court began the confirmation hearing on the Debtor's Plan and Heartland's Motion to Convert or Dismiss. The confirmation hearing continued over a period of five days on January 23, 24, 25 and 28, and March 14, 1991. Closing arguments were made by the parties at the close of the confirmation hearing on March 14, 1991.

9. Upon consideration of the Plan and the Objection filed by Heartland, and the Court having considered and admitted into evidence for purposes of the

confirmation hearing, the documents identified in the exhibit lists filed by the Debtor and Heartland, together with the pleadings and other papers filed in this case, and the evidence and arguments of counsel having been presented to this Court, in accordance with Bankruptcy Rules 7052 and 9014, the Court makes the following Findings of Fact and Conclusions of Law:

FINDINGS OF FACT AND CONCLUSIONS OF LAW

10. This Court has jurisdiction over this case. Confirmation of the Plan and Heartland's Motion to Convert or Dismiss are "core" matters. 11 U.S.C. § 1129; 28 U.S.C. § 157(b)(1), § 157(b)(2)(A), (L), (O), and § 1334.

11. The modifications to the Plan, which were included in the Plan after voting thereon, but prior to confirmation, do not adversely change the treatment of the claim of any creditor of the Debtor. See Bankruptcy Rule 3018.

Section 1129(a)(1)

12. The Plan complies with the applicable provisions of the Bankruptcy Code.

13. Article 3 of the Plan designates six (6) separate classes of claims and interests. 11 U.S.C. § 1123(a)(1). The claims and interests in each class are based upon separate and distinct legal natures. Therefore, a reasonable basis exists for separate classifications of these claims and interests. The claims and interests in each class under the Plan are substantially similar and their classification satisfies the requirements of § 1122(a)

of the Bankruptcy Code.

14. Heartland objected to the Plan on the grounds that the Plan did not specify whether the Administrative Claims or the Priority Claims are impaired. Such a designation with respect to Administrative Claims and Priority Claims is unnecessary. Pursuant to 11 U.S.C. § 1129(a)(9) of the Bankruptcy Code, the Administrative Claims and Priority Claims cannot be impaired. The class of interest holders is also not specified as unimpaired. Such a designation is meaningless because the interest holders did not receive or retain any property under the Plan and, hence, are deemed not to have accepted the Plan. 11 U.S.C. §1126(g).

15. Heartland also objected to the Plan on the grounds that both its deficiency claim and its secured claim were included in one class. If Heartland had made an election under §1111(b) election, its unsecured claim should technically have been classified separately from its secured claim. The Court accepted the Plan which provided for separate classification of Heartland's secured and unsecured claims. Heartland's secured claim will receive the treatment provided in Class 4 while its unsecured claim will receive the same treatment as provided in Class 5. Two unsecured classes of non-insider creditors voted to accept the Plan; thus, the control of two classes by Heartland effectuates a non-substantive and technical amendment to the Plan. The Court recognizes the "well established principle that relief under bankruptcy laws is not to be withheld because of technicalities." Kane v. Johns-Manville, (In re Johns-Manville), 843 F.2d 636, 648 (2nd Cir. 1988) (cite omitted). Heartland's objections to confirmation of the Plan based on technical issues relating to classification are overruled.

16. Article 4 of the Plan describes the treatment to be afforded to each of the impaired classes. 11 U.S.C. § 1123(a)(3).

17. Article 5 of the Plan provides adequate means for execution and implementation of the Plan. 11 U.S.C. § 1123(a)(5). Section 5.2 of the Plan provides that at closing, the Regalridge Trust will be established for the purposes of owning, managing, and operating the Property. The property will be transferred to the Regalridge Trust upon the effective date. The Plan further provides that all interests in the Debtor will be deemed cancelled.

18. The Plan further provides that on the effective date, the Regalridge Trust will be executed by the Debtor and the Regalridge Trustees. The Plan provides for the appointment of three (3) Regalridge Trustees to hold and manage the Property. The Regalridge Trustees will be appointed one each by the City of Fort Worth, the Fort Worth NAACP, and Heartland. The third Regalridge Trustee will be appointed by Heartland. The Plan also specifies the minimum qualifications for the Regalridge Trustees. Each Regalridge Trustee must be (a) a resident of the City of Fort Worth; (b) at least 35 years of age; (c) uninvolved in any business or partnership with Leonard E. Briscoe, Sr. or the Debtor; and (d) unrelated to and not a close personal friend of Leonard E. Briscoe, Sr. The Plan further provides that the Regalridge Trustees will receive no compensation for their services but may receive reimbursement of their actual and necessary expenses incurred in carrying out their responsibilities under the Trust. In addition, the Regalridge Trustees will serve without bond. The Court finds that the provisions of the Plan regarding the selection of the Regalridge Trustees are consistent with the interest of creditors and with public

policy.

19. The Plan provides for the distribution to creditors on a pro rata basis of the cash flow on at least an annual basis.

20. The Plan provides for the transfer of the Property to the Regalridge Trust, which is not a corporation. Thus, § 1123(a)(6), made applicable to this case by § 1129(a)(1), is not applicable.

21. The manner and selection of the Regalridge Trustees is consistent with the interests of creditors and with public policy. The Debtor has disclosed the identity and affiliation of the Regalridge Trustees who have been appointed by the Fort Worth NAACP and the City of Fort Worth. The appointment and qualifications of the Regalridge Trustees are consistent with the interests of creditors and public policy.

Section 1129(a)(3)

22. The Plan has been proposed in good faith and not by any means forbidden by law. 11 U.S.C. §1129(a)(3). In order to determine whether a plan has been proposed in good faith, the Court must look to the totality of the circumstances surrounding the formation of the Plan. In re Texas Extrusion Corp., 844 F.2d 1142, 1160 (5th Cir.), cert. denied, 488 U.S. 926 (1988). A plan proposed with a legitimate and honest purposes, and which has a reasonable hope of success, satisfies the good faith requirement. In re Sun Country Dev., Inc., 764 F.2d at 408 (5th Cir. 1985). The Plan provides a vehicle for restructuring the debt of the Property and preserving the Property for the benefit of both creditors and the Fort

Worth community. Moreover, none of the interest holders of the Debtor will retain anything under the Plan. Consequently, the Plan has been proposed in good faith and not by any means forbidden by law.

Section 1129(a)(4)

23. Section 1129(a)(4) requires that payments for services or for costs and expenses in and in connection with the case, or in connection with the Plan and incident to the case, either have been approved by the Court as reasonable or are subject to approval of the Court as reasonable. Interim payments remain subject to review and approval by this Court on final application. The Plan provides that any other payments falling within the parameters of § 1129(a)(4) will not be made without Court approval.

Section 1129(a)(5)

24. Section 1129(a)(5) requires the Debtor to disclose the identity of certain individuals who will hold positions with the Debtor or its successor after confirmation of the Plan. The Debtor will not retain any interest in the Property after confirmation. Instead, Regalridge Trustees will be appointed to administer the Regalridge Trust which will own and hold the Property. The appointment of the Regalridge Trustees pursuant to the provisions of the Plan and as discussed herein is consistent with the interests of creditors and public policy.

Section 1129(a)(6)

25. There are no rates applicable to the Debtor's business over which any regulatory commission

will have jurisdiction after confirmation. 11 U.S.C. § 1129(a)(6).

Section 1129(a)(7)

26. The Plan satisfies the requirements of §1129(a)(7), the best interests of creditors test. Under the Plan, Classes 3, 4 and 5 are impaired. With respect to Classes 3 and 5, each voting holder of a claim in such class will receive or retain under the Plan on account of the claim property of a value, as of the effective date, that is not less than the amount that each holder would receive or retain if the Debtor were instead liquidated under Chapter 7 of the Bankruptcy Code on the effective date or has accepted the Plan.

27. With respect to satisfaction of §1129(a)(7) regarding the claims of Heartland, the Debtor presented evidence to the Court which shows that the Property will probably support debt service equal to Heartland's secured claim of $8.2 million. In other words, Heartland will receive the present value of its secured claim. In addition, the Court finds, based on the evidence presented, that over the next six years, money will be available as cash flow for distribution to creditors whose claims will be treated as unsecured Class 5 claims after payment of ordinary and necessary operating expenses and payment of debt service on Heartland's secured claim. The unsecured deficiency claim of Heartland, which is approximately $10 million, will receive the same treatment provided for Class 5 claims. The Debtor provided additional evidence which showed that in the event of liquidation in a Chapter 7 case, only the priority claim of the City of Fort Worth and the secured claim of Heartland (Classes 2 and 4, respectively) would receive any consideration.

Consequently, in a Chapter 7 liquidation case, no amounts would be available for distribution to creditors whose claims are treated as unsecured Class 5 claims under the Plan.

Section 1129(a)(8)

28. Section 1129(a)(8) requires that each impaired class of claims or interests have accepted the Plan. The City of Fort Worth timely file a ballot to accept the Plan based upon its Class 2 claim. The Court finds that based on Ballots filed with this Court, the City of Fort Worth voted its impaired Class 3 claim to accept the Plan. The unsecured Class 3 claim of the City of Fort Worth exceeds $7 million. The Court also finds that: (i) six Class 5 creditors also timely filed ballots to accept the Plan; (ii) five additional Class 5 creditors voted to accept the Plan, but such ballots were received after the deadline for filing the ballots; and (iii) no Class 5 creditors voted against the Plan. After considering the evidence presented, the Court finds that based upon the timely filed Ballots by Class 3 and Class 5 creditors, such claims are sufficient in number and amount to constitute acceptance by such classes of the Plan pursuant to 11 U.S.C. §1126. Because both the unsecured and secured claims of Heartland voted to reject the Plan, the Plan does not satisfy the requirements of §1129(a)(8). The holders of interests in Class 6 will neither receive nor retain property under the Plan, and therefore, are deemed to have rejected the Plan. 11 U.S.C. §1126(g).

Section 1129(a)(9)

29. Section 1129(a)(9) contains a number of requirements concerning the payment of priority claims.

The Plan meets the requirements of two subsections of Section 1129(a)(9) by providing for payment in full of priority claims in cash on or before the later of the effective date of the Plan and the date a priority claim is allowed.

Section 1129(a)(10)

30. The holders of claims in at least one impaired class under the Plan have accepted the Plan, determined without including any acceptance of the Plan by an insider of the Debtor which holds a claim in that class. In this case, Class 3, an impaired class, has voted to accept the Plan. None of the creditors in Class 3 are insiders within the meaning of §1129(a)(10).

Section 1129(a)(11)

31. The Plan is feasible and has a marginal prospect of success. The reorganized Debtor is capable of performing under the Plan and confirmation will not likely be followed by the need for further financial reorganization or liquidation of the Debtor or its successor except to the extent that the Plan provides for liquidation and reorganization.

32. The Plan contemplates the use of operating revenue for the success of the Plan. In order to determine whether the Plan is feasible, the Court is required to determine (a) the value of Heartland's secured claims; and (b) the likelihood that the Property can generate sufficient cash flow to pay its ordinary and necessary operating expenses, meet debt service and produce a surplus for distribution to creditors.

33. Section 506(a) of the Bankruptcy Code provides that an allowed claim of a creditor secured by a lien on property in which the estate has an interest is secured to the extent of the value of that creditor's interest in such property and is an unsecured claim to the extent that the value of the creditor's interest is less than the amount of its allowed claim. The value of the creditor's secured claim is to be determined in light of the purpose of the valuation and the proposed disposition of the Property.

34. In the instant case, the Debtor has approximately $750,000 in pre-petition ad valorem taxes which upon sale or other disposition of the Property would be paid before Heartland's secured claim. In addition, the Debtor presented evidence that approximately $250,000 to $300,000 is needed to make repairs on the Property.

35. The Debtor presented evidence by its appraiser, James Daniels, MAI, that the value of the Property is $9.2 million, if the taxes are paid and if the needed repairs have been made. The Court finds Mr. Daniels' testimony credible and convincing, and therefore, finds that the value of the Property, as is, that is after taking into consideration the $750,000 tax lien held by the City of Fort Worth that will not be paid in full at confirmation, and after making a deduction for repairs, is $8.2 million. See Transcript of Hearing, pp. 38-55. The Court finds that the value of Heartland's secured claim is $8.2 million.

36. The Debtor's financial projections showed that with income of $200,000 per month, the Property will generate sufficient cash flow to pay: (i) necessary and normal operating expenses; (ii) the secured debt of

Heartland at a market rate of interest; and (iii) a dividend to creditors whose claims are treated as Class 5 claims on at least an annual basis. The Debtor's evidence further showed that for the past several months, the Debtor has met or exceeded the $200,000 per month income that will be needed to fund the Plan. The evidence further showed that occupancy at the Property has increased from approximately 55% at the commencement of the case to its current level of 85%. The Debtor presented further evidence that occupancy at the Property will probably increase to approximately 90% within the first half of this year. The Court accepts the Debtor's projections but cautions that the Debtor will have to work diligently to make this Plan succeed.

37. The Debtor also has demonstrated its ability to make the needed repairs on the Property. Prior to the continuation of the confirmation hearing on March 14, 1991, counsel for the Debtor and Heartland announced to the Court a resolution of the adversary proceeding filed by the Debtor against Heartland for turnover of certain insurance proceeds in order to make the repairs on the Property. Pursuant to the agreement reached by the parties, Heartland has consented to the Debtor's use of approximately $225,000 of insurance proceeds not only to make repairs on the Property that are covered by the insurance proceeds but also to use any excess insurance proceeds to make additional repairs on the Property. While some of the repairs are urgent in nature, the Debtor presented testimony that some of the repairs could be delayed throughout the remainder of the year and that such deferred repairs could be paid for from cash flow that will be available by the end of the year.

38. Based on the evidence presented herein, the Court finds that the Plan is not likely to be followed by the need for further financial reorganization or liquidation and is feasible.

Section 1129(a)(12)

39. All fees payable under 28 U.S.C. § 1930, and determined by the Court at the confirmation hearing, have been paid or the Plan provides for such payment.

Section 1129(a)(13)

40. The Debtor has no retiree plans, funds, or programs that provide for the payment of retiree benefits as defined in § 1141 of the Bankruptcy Code.

Section 1129(b)

41. Heartland voted its secured and unsecured claims to reject the Plan. Notwithstanding such rejection, the Plan may be confirmed pursuant to § 1129(b) of the Bankruptcy Code because the Plan satisfies the requirements of § 1129(a) except subparagraph (a)(8), does not discriminate unfairly against Heartland, and is fair and equitable.

42. The Plan is fair and equitable to Heartland because Heartland will retain the lien securing its claim and will receive on account of its claims deferred cash payments totaling at least the allowed amount of its claim of a value, as of the effective date of at least the value of Heartland's interest in the Property. The Plan provides that Heartland's secured claim will be paid in monthly

installments of principal and interest as though amortized over thirty years. Interest on the secured claim will be paid at the rate of ten and one-quarter percent (10.25%) per annum which is the same rate of interest included in the January 31, 1984 promissory note from the Debtor to Heartland (or its Predecessor). The outstanding principal balance of Heartland's secured claim will be paid on the earlier date of the sale of the Property or the expiration of fifteen (15) years after the effective date. Based upon the evidence presented at the confirmation hearing, the Court finds that the rate of interest to be paid to Heartland on account of its secured claim together with the scheduled amortizing payments of principal to be made pursuant to the Plan will provide Heartland with payments totalling the present value of its secured claim.

43. Moreover, the treatment of Heartland's deficiency claim in Class 5 is identical to the treatment of all creditors whose claims are being treated in Class 5. Thus, the Plan protects the legal rights of Heartland's unsecured deficiency claim consistent with the treatment afforded to the accepting unsecured Class 3 and Class 5 claims. The Plan also is fair and equitable to the unsecured and secured claims of Heartland because no holder of any claim or interest junior to Heartland's claims under the Plan will receive or retain on account of the junior claim or interest any property under the Plan. In addition, implicit in the fair and equitable standard of §1129(b) is the requirement that single claims not receive a recovery greater than 100% of their claims, based on the evaluation of distribution at the time of the confirmation hearing. No class of holders of claims that are senior to the Class 4 claim under the Plan will receive distribution having the value determined as of the time of the confirmation hearing in excess of the allowed amount of

such holder's claim.

SUMMARY

Based upon the foregoing Findings of Fact and Conclusions of Law, it is appropriate for this Court to CONFIRM Debtor's Fourth Amended Plan of Reorganization, Overrule Heartland's Objections to such Plan and Deny Heartland's Motion to Dismiss or Convert.

All further relief not expressly granted herein is denied.

This Court shall enter an Order in conformity with the Findings of Fact and Conclusions of Law entered this date.

IT IS SO ORDERED.

SIGNED: April 23, 1991

s/Massie Tillman
Honorable Massie Tillman
United States Bankruptcy Judge

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 92-1446

In re: Briscoe Enterprises, Ltd., II,
d/b/a Regalridge Apartments,

Debtor.

Heartland Federal Savings & Loan Association,

Appellee,

vs.

Briscoe Enterprises, Ltd., II,
d/b/a Regalridge Apartments,

Appellant.

On Petition for Rehearing and Suggestion
for Rehearing En Banc

Before Wisdom and Duhe', Circuit Judges, and Doherty*, District Judge.

*District Judge of the Western District of Louisiana, sitting by designation.

Per curiam:

The petition for Rehearing is DENIED and no member of this panel nor Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc, (Federal Rules of Appellate Procedure and Local Rule 35) the Suggestion for Rehearing En Banc is DENIED.

Entered for the Court:
s/John Minor Wisdom
United States Circuit Judge
August 16, 1993

Judges Barksdale, King and Jones did not participate in the consideration of the suggestion for rehearing en banc.

* * * * * * * * * *

Respectfully submitted,

Douglas S. Lang
Deirdre Ruckman
Stacy R. Obenhaus*
GARDERE & WYNNE, L.L.P.
3000 Thanksgiving Tower
Dallas, Texas 75201
(214) 999-3000

Attorneys for Petitioner
*Counsel of Record

(3)

Supreme Court, U.S.
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No. 93-516

In The

Supreme Court of the United States

October Term, 1993

HEARTLAND FEDERAL SAVINGS AND LOAN ASSOCIATION,

Petitioner,

vs.

BRISCOE ENTERPRISES, LTD., II,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

RALPH I. MILLER*
CRAIG H. AVERCH
RUTH L. RICKARD
WEIL, GOTSHAL & MANGES
100 Crescent Court, Suite 1300
Dallas, Texas 75201-6950
(214) 746-7700

Attorneys for Respondent
*Counsel of Record

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
OR CALL COLLECT (402) 342-2831

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QUESTIONS PRESENTED

This case involves a chapter 11 plan of reorganization that was confirmed under the "cramdown" provisions of 11 U.S.C. § 1129(b), and which confirmation was affirmed by the Fifth Circuit Court of Appeals.

1. Should this Court grant a writ of certiorari where the Fifth Circuit Court of Appeals has applied the *preponderance of the evidence* standard to 11 U.S.C. § 1129(b) consistent with decisions of this Court, and where the Court of Appeals Opinion below is the only circuit court decision to determine this issue.

2. Should this Court grant a writ of certiorari where the Fifth Circuit Court of Appeals, after reviewing the record evidence heard by the bankruptcy court, found that the proponent of the plan of reorganization met its burden of proof under the "fair and equitable" standard of 11 U.S.C. § 1129(b).

3. Should this Court grant a writ of certiorari to determine whether to adopt a *per se* rule requiring different treatment of similar but separately classified claims when no circuit court has adopted a *per se* rule.

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No. 93-516

In The

Supreme Court of the United States

October Term, 1993

HEARTLAND FEDERAL SAVINGS AND LOAN ASSOCIATION,

Petitioner,

vs.

BRISCOE ENTERPRISES, LTD., II,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

TO THE UNITED STATES SUPREME COURT:

Briscoe Enterprises, Ltd., II ("Briscoe") files this Brief in Opposition to Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit ("Response"), asking this Court to deny the petition for writ of certiorari ("Petition") to review the opinion issued July 13, 1993 by the United States Court of Appeals for the Fifth Circuit. In support of this request, Briscoe would respectfully show the Court as follows:

JURISDICTION

In addition to the jurisdictional facts listed by Heartland, Briscoe notes that the bankruptcy court had jurisdiction to confirm Briscoe's plan of reorganization pursuant to both 28 U.S.C. § 1334 and § 157. With respect to the appellate court decision at issue, the Fifth Circuit denied both Heartland's Motion for Rehearing and its Suggestion for Rehearing *En Banc* on August 16, 1993. *Briscoe Enters., Ltd., II v. Heartland Fed. Sav. & Loan Ass'n (In re Briscoe)*, 994 F.2d 1160 (5th Cir. 1993); Pet. App. at 1-26 (the "Court of Appeals Opinion").

STATEMENT OF THE CASE

Briscoe owns and operates Regalridge Square Apartments ("Regalridge" or the "Property"), a 784-unit apartment complex located in southeast Fort Worth, Texas. Regalridge serves low- to moderate-income families, many of whom receive rental subsidies from the federal government. In addition, the City of Fort Worth (the "City"), through its Rental Assistance Program, contributes approximately $20,000 a month for rental subsidies on behalf of Regalridge residents.

Briscoe's Plan of Reorganization (the "Plan") provides generally for continued operation of Regalridge as a quality residential community for a largely African-American population and for payment of creditor claims. On the effective date of the Plan, the Regalridge property will be transferred to the Regalridge Trust for the benefit of creditors. The Regalridge Trust will be managed by a panel of three trustees, one each appointed by Heartland,

the City, and the Fort Worth NAACP. All equity interests in Briscoe will be cancelled, and interest holders will receive nothing under the Plan. The Plan also provides for creation of a Distribution Fund (as defined in the Plan), by which the City may provide approximately $150,000 for additional tenant subsidies in the future.

In its Petition, Heartland misstates several facts concerning the classification scheme and voting, although Briscoe would point out that these do not affect the gravamen of Heartland's complaint, *i.e.*, that the City's unsecured claim was treated the same, but classified separately from the other unsecured claims.

Heartland misstates that its unsecured claim was placed with that of other unsecured claims in Class 5 and that Class 5 voted against the Plan. Pet. at 6, 17. The facts as stated in the Court of Appeals Opinion are correct. Heartland's entire claim (both the secured and unsecured portion) was placed in Class 4 (which voted against the Plan), but the unsecured portion of Heartland's claim would be treated like that of the unsecured claims in Class 5. 994 F.2d at 1163; Pet. App. at 4-5. Class 5 (other unsecured claims), as well as Class 3 (the City's unsecured claim) and Class 2 (the City's secured ad valorem tax claim) voted for the Plan.

The bankruptcy court conducted five days of hearings that included testimony from eight witnesses. The bankruptcy judge conducted a personal inspection of the property with counsel present. 994 F.2d at 1162; Pet. App. at 3. Based on this evidence, the bankruptcy court found that Respondent Briscoe had met its burden of proof and confirmed the Plan. The district court reversed, but the

Fifth Circuit Court of Appeals, in a unanimous nine-page opinion authored by Judge Wisdom, reversed the district court and affirmed the confirmation order of the bankruptcy court.

SUMMARY OF THE ARGUMENT

The Fifth Circuit's application of the preponderance of the evidence standard to the cramdown provisions of the Bankruptcy Code does not warrant review by this Court because the decision correctly applies this Court's precedent and there is no circuit conflict. The opinion of the Court of Appeals is the only circuit court decision that determines what standard of proof applies to cramdown.

The Fifth Circuit did not shift the burden of proving the reorganization plan was fair and equitable from Briscoe, the plan proponent, to Heartland. In a supplemental letter brief to the Fifth Circuit, Briscoe summarized and cited relevant evidence it had presented in four days of hearings. In reaching its conclusion that the Plan was fair and equitable to Heartland, the Court of Appeals Opinion adverts to "the evidence presented to the bankruptcy court" and discusses specific relevant facts, *e.g.*, whether the interest rate would adequately compensate Heartland and that Heartland had the right to foreclose under the plan.

Heartland requests this Court to engraft a *per se* rule that, to justify classifying similar claims separately, the plan proponent must treat the classes differently. The issue is not worthy of review for a number of reasons.

There is no conflict between the circuits: each one to address this issue has recognized that good reasons may exist to justify separate classification. None of the circuits, however, has adopted a *per se* rule that such claims must receive different treatment (a purported indicator that "good reasons" exist to classify similar claims separately). Moreover, the proposed rule is misguided and does not prevent the mischief to be avoided – that of improper classification for the purpose of obtaining an affirmative class vote to enable the proponent to use the cramdown provisions. There is no need for this Court to intervene, because the circuit courts are harmoniously developing, on a case-by-case basis, the contours of the "good reasons" test to justify classifying similar claims separately. Finally, unique facts make this case an inappropriate candidate for certiorari to consider separate classification law because the creditor classified separately was the City of Fort Worth, which has non-creditor interests related to urban housing and which contributes $20,000 per month in rental assistance.

ARGUMENT

I. THE STANDARD OF PROOF ISSUE DOES NOT WARRANT REVIEW BY THIS COURT

The Fifth Circuit's application of the preponderance of the evidence standard to the cramdown provisions of the Bankruptcy Code does not warrant review by this Court. The decision does not conflict with any other circuit court opinion. Furthermore, the Court of Appeals

correctly applied this Court's holdings in *Grogan v. Garner*, 498 U.S. 279 (1991) and *Addington v. Texas*, 441 U.S. 418 (1979). Moreover, the decision here is in full accord with the only circuit-level decision applying *Grogan*.

A. THERE IS NO CONFLICT BETWEEN THE FIFTH CIRCUIT'S DECISION AND DECISIONS OF OTHER CIRCUIT COURTS

In an effort to create the appearance of conflict with other circuits, Heartland cites a string of seven decisions for the proposition that clear and convincing proof is required in a cramdown. None of these is a circuit court decision. Further, none of the seven decisions includes a reasoned discussion or any explanation of why the appropriate evidentiary standard should be more than a preponderance. Indeed, the Court of Appeals Opinion is the *only* decision that applies *Grogan* in analyzing what standard of proof applies to section 1129 of the Bankruptcy Code.[1]

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[1] Heartland asserts that there is a "risk of confusion" because of decisions applying the clear and convincing standard in the context of particular contested matters in a bankruptcy case. This assertion is without merit because the cases cited by Heartland were either decided before *Grogan* or do not involve the application of a provision of the Bankruptcy Code. For example, *In re Vermont Toy Works, Inc.*, 135 B.R. 762 (D. Vt. 1991) involved the application of *state law* – the common law of marshalling – in a bankruptcy case.

B. APPLYING THE PREPONDERANCE STANDARD TO CRAMDOWN IS THE LOGICAL EXTENSION OF THE *GROGAN* DECISION

In *Grogan*, this Court held that the preponderance standard is applicable in actions to determine whether particular debts are dischargeable under 11 U.S.C. section 523. In reaching this conclusion, the Court noted that the statute and legislative history were silent concerning the standard of proof and further stated that

> [T]his silence is inconsistent with the view that Congress intended to require a special, heightened standard of proof. Because the preponderance of the evidence standard results in a roughly equal allocation of the risk of error between litigants, we presume that this standard is applicable in civil actions between private litigants unless "particularly important individual interests or rights are at stake."

Grogan, 498 U.S. at 286 (citing *Herman & MacLean v. Huddleston*, 459 U.S. 375 (1983) and *Addington v. Texas*, 441 U.S. 418 (1979)). Even though the clear and convincing standard had historically been applied in fraud cases, this Court found no "important individual interests" at stake and held that preponderance of the evidence is the appropriate standard under section 523 of the Bankruptcy Code. *Id.*

Following the reasoning process in *Grogan*, the Court of Appeals noted that the language of section 1129 and the legislative history were silent on the applicable burden of proof. After discussing *Herman & MacLean* and *Addington*, the Court of Appeals found no interests at stake that would trigger a heightened standard of proof,

concluding that this case is "solely about money."[2] 994 F.2d at 1164-65; Pet. App. at 8-11. As in *Grogan*, the Court of Appeals concluded that a heightened standard of proof above that of a preponderance of the evidence was not warranted.[3]

C. RATHER THAN CONFLICT WITH OTHER CIRCUITS, THE FIFTH CIRCUIT AND TENTH CIRCUIT HAVE FOLLOWED *GROGAN* TO THE SAME EFFECT

Far from creating a conflict, the Court of Appeals Opinion is fully in accord with existing law in other circuits. In *First National Bank v. Serafini*, 938 F.2d 1156 (10th Cir. 1991), the Tenth Circuit held that the preponderance standard, not the clear and convincing standard, is the appropriate standard in a dischargeability action brought pursuant to 11 U.S.C. section 727. *Id.* at 1157. Even though *Serafini* involved the discharge of a debtor under section 727, and not the dischargeability of a debt under section 523 as in *Grogan*, the Tenth Circuit stated that "we perceive no good reason to apply a different standard where § 727(a)(2) is involved." *Id.* Thus, the circuit courts that have applied *Grogan* are in complete

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[2] This language adverts to Chief Justice Burger's language in *Addington*, where he noted that the clear and convincing standard had been employed in civil cases when "the interests at stake are deemed to be more substantial than mere loss of money." 994 F.2d at 1164; Pet. App. at 8.

[3] If this Court wishes to signal that the Fifth Circuit properly applied *Grogan*, it could efficiently do so through a summary affirmance of the Court of Appeals Opinion under Rule 16.1 of the Rules of the Supreme Court.

agreement: if the statutory language and legislative history are silent as to the appropriate standard of proof and the interests at stake are not important individual interests, the ordinary preponderance standard applies.

II. THE FIFTH CIRCUIT DID NOT SHIFT THE BURDEN OF PROOF ON WHETHER A PLAN IS "FAIR AND EQUITABLE" ONTO THE PLAN OPPONENT

The Fifth Circuit did not shift from Briscoe to Heartland the burden of proving whether a plan is fair and equitable. The issue that Heartland raises is, in essence, a sufficiency of the evidence issue that is wholly unworthy of review by this Court.

The Court of Appeals Opinion shows that the court below relied on pertinent record evidence in concluding that Briscoe had met the cramdown requirements. 994 F.2d at 1169; Pet. App. at 20-23. The Court of Appeals explicitly adverted to the "evidence presented to the bankruptcy court" in its discussion preceding its conclusion that "the plan satisfies 1129(b)(2)(A)(i) [the "fair and equitable" requirement]." *Id.* Briscoe produced the relevant facts during a five-day hearing. Pertinent record evidence was explicitly detailed to the appellate court. *See* Resp. App. at 3-5.[4]

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[4] Supplemental to the briefing below, the appellate court invited the parties to respond to the views of Professor Warren. Briscoe's response was in a letter from Marilyn D. Garner to Susan Vaughn, which is reprinted in the Respondent's Appendix (hereinafter "Resp. App."). A portion of that response summarizes numerous record facts about Regalridge.

The essence of Heartland's argument is not that the court shifted the burden of proof, but that Briscoe's evidence was insufficient to establish fair and equitable treatment of Heartland. Indeed, Heartland admits in its Petition that "The [appellate] court determined that Briscoe had proved all the elements of the case" under the preponderance of the evidence standard. Pet. at 7. Heartland's argument below (and its real complaint here) was that the lower courts refused to *require* Briscoe to produce affirmative evidence of the value of the property in fifteen years. In fact, the appellate court specifically cautioned that any evidence of value in fifteen years was "inherently speculative." *Id.* The court, instead, sensibly focused upon immediate facts relevant to the issue of fairness, *i.e.*, that the interest rate was generous and that Heartland could foreclose if the reorganized debtor failed to service its debt.[5]

The passage from the Court of Appeals Opinion that troubles Heartland warrants quotation in full:

> Heartland and the district court suggest that allowing a balloon payment is unacceptable as there is no immediate indication from where the funds will come to pay off the balloon. As a

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[5] After carefully considering the record on appeal, the Court of Appeals concluded that 1) the Plan ensured that Heartland would have the right to foreclose if Briscoe failed to pay its debt service obligations, and 2) that the bankruptcy court's finding that a 10.25% interest rate adequately compensated Heartland for its risk was not clearly erroneous. The Court of Appeals then specifically acknowledged that the balloon payment added "some measure of risk," but concluded that "the interest rate appears adequate to cover this risk." 994 F.2d at 1168; Pet. App. at 22.

> general matter, many courts have held balloon payments to satisfy 1129(b).[6] It is reasonable to assume that the property itself will provide the source for the balloon payment.[7] There is no evidence that the property will decline in value. Therefore, when the balloon is due, either the property will be sold which will provide the balloon or refinancing will be possible. *Estimating property values fifteen years hence is inherently speculative, but the evidence presented to the bankruptcy court did not suggest that the property would decline in value so that the debtor would be unable to pay Heartland its remaining principal.* Therefore, we hold that the plan satisfies 1129(b)(2)(A)(i).

994 F.2d at 1169; Pet. App. at 22-23 (emphasis supplied).

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[6] In support, the Court of Appeals cites, in footnote 51, *In re Bryson Properties, XVIII*, 961 F.2d 496, 501 (4th Cir.), *cert. denied*, 113 S. Ct. 191 (1992) and *In re Guildford Telecasters, Inc.*, 128 B.R. 622, 627 (Bankr. M.D.N.C. 1991).

[7] Heartland would also imply that the appellate court based its decision upon an insupportable assumption, seizing upon the language that the court "assumed" that the property would provide the source for the balloon payment. Read in context, it is clear that this comment is in response to an argument raised by Heartland below. Heartland had argued that allowing a balloon payment was unacceptable as there was no immediate indication where the funds would come from to pay off the balloon. In the context of this single asset real estate case, where Heartland retains its senior lien, the appellate court gave this argument short shrift, stating "It is reasonable to assume that the property itself will provide the source for the balloon payment."

The emphasized passage makes clear that the court reviewed the *evidence presented to the bankruptcy court*.[8] That included, for example, Briscoe's evidence concerning the minimum income required to fund the Plan, historic income levels and occupancy levels in the apartment complex, and data concerning budget items, taxes and repairs. Resp. App. at 3-5.

Thus, the appellate court did not shift the burden of proof. Heartland has shown no grounds of error in the appellate court's careful examination of this fact-bound determination, let alone grounds that warrant review by this Court. While Heartland may take issue with the Fifth Circuit's determination that the Plan was "fair and equitable," it cannot maintain that the burden of proof was shifted away from Briscoe and onto Heartland. For these reasons, the Petition should be denied.

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[8] Heartland had raised the issue whether the Plan was "fair and equitable" as required under section 1129(b) because Heartland feared the Property would decline in value before it received full payment on its claim. Briscoe explained to the appellate court that "While it is true that the Bankruptcy Court did not make a specific finding regarding the value of the Property fifteen years after confirmation, the Bankruptcy Court had before it credible evidence that the Property would not decline in value." Letter from Marilyn D. Garner to Susan Vaughn, Resp. App. at 3.

III. THE COURT OF APPEALS OPINION REGARDING SEPARATE CLASSIFICATION IS CONSISTENT WITH *GREYSTONE* AND DOES NOT CONFLICT WITH OTHER CIRCUIT COURT DECISIONS

The circuit court decisions are uniform on the issue of separate classification. Each circuit that has addressed the issue has recognized that good reasons may exist to justify separate classification of similar claims. *See In re Greystone III Joint Venture*, 948 F.2d 134 (5th Cir.), *cert. denied*, 113 S. Ct. 72 (1992); *John Hancock Mut. Life Ins. Co. v. Route 37 Business Park Assocs.*, 987 F.2d 154, 161-62 (3d Cir. 1993) (separate classification based on distinction relating to recourse debt differences and proffered business reasons was not justified, but good reasons may exist to justify separate classification); *Lumber Exchange Bldg. Ltd. Partnership v. Mutual Life Ins. Co.*, 968 F.2d 647, 649 (8th Cir. 1992) ("A debtor may classify substantially similar claims separately for reasons independent of the debtor's motivation to secure the vote of an impaired class of claims," citing *Greystone*); *In re Bryson Properties, XVIII*, 961 F.2d 496, 502 (4th Cir.), *cert. denied*, 113 S. Ct. 191 (1992) (separate classification is sustainable if sufficient justification exists, but refusing to sustain separate classification based on "natural" and "unnatural" recourse distinction); *In re U.S. Truck*, 800 F.2d 581, 587 (6th Cir. 1986) (separate classification permitted where the interests of creditors differ substantially; interests other than payment of debt were at stake). Heartland asks this Court to engraft onto the "good reasons" exception a *per se* rule that when similar claims are classified

separately, the plan must treat them differently. No circuit court has adopted this rule, and for good reason.[9]

Heartland presents no cases showing a conflict between the circuits on this issue. Heartland is incorrect insofar as it suggests that there is a conflict between the Court of Appeals Opinion and the Fourth Circuit decision in *Bryson*. Both the Court of Appeals and the *Bryson* court rejected a *per se* rule that would require different treatment of separately classified claims. Furthermore, the Fifth Circuit's denial of the Suggestion for Rehearing *En*

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[9] The proposed rule would not prevent the mischief to be avoided – that of *improper* classification of similar claims to obtain an affirming vote in a cramdown situation. Indeed, the proposed rule itself is subject to manipulation: plan proponents could merely treat separately classified claims differently, whether or not such is necessary, and whether or not there is an improper purpose to gerrymander. Rather than clutter the analysis with a misguided rule, the courts have generally focused on the right question: whether the proposed classification scheme, under the particular facts, constitutes improper manipulation. For example, the Third Circuit requires that the classification scheme be "reasonable" and that "each class must represent a voting interest that is sufficiently distinct and weighty to merit a separate voice in the decision whether a proposed reorganization should proceed." *Route 37 Business Park Assocs.*, 987 F.2d at 159.

Banc dispels any notion that *Greystone* adopted a *per se* rule.[10]

Specifically, in *Bryson*, the Fourth Circuit deemed that according the same treatment to separately classified unsecured claims is "highly suspect." 961 F.2d at 500. Nevertheless, the court explicitly entertained the possibility that the debtor (the plan proponent) could offer reasons for the separate classification that would "withstand scrutiny." *Id.*

Similarly, the Court of Appeals here merely applied the "good reasons" exception in a manner consistent with *Bryson*. That is, the Court of Appeals first acknowledged the general rule of *Greystone* that "thou shalt not classify similar claims differently in order to gerrymander an affirmative vote on a reorganization plan." 994 F.2d at 1167; Pet. App. at 15. Following the Sixth Circuit in *U.S. Truck*, the Court of Appeals explicitly discussed the

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[10] Heartland misreads *Greystone* to require that "good business reasons" are valid only if the different classes receive different treatment under the plan. Pet. at 18. The passage in *Greystone* upon which Heartland relies is dicta and far from an iron clad rule: "Because there is no separate treatment of the trade creditors *in this case*, we reject Greystone's 'realities of business' argument." 948 F.2d at 141 (emphasis added). Moreover, it is clear that the panel below and the Fifth Circuit *en banc* perceived no need to "correct" or even clarify the Panel Opinion, in that both the Petition for Rehearing and the Suggestion for Rehearing *En Banc* were denied.

distinct interest of the City,[11] specifically its non-creditor interests and its contribution of $20,000 a month relating to its urban housing program. 994 F.2d at 1167; Pet. App.

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[11] The City's considerable non-creditor interest in the Property is evident from the following excerpt from closing arguments:

MR. COLVIN: I'll be very brief, Your Honor. Your Honor, the City of Fort Worth through the Trinity Housing Authority has invested in excess of $8 million into this project. This investment was made in order to have built in the city a safe low to moderate income project. We believe that the property and its preservation as a safe low to moderate income property is paramount, at least in the eyes of the City, and for this reason the City voted its unsecured claim in favor of the Plan.

Your Honor, we believe the Plan is feasible. We think the value is as represented by the Debtor.

Your Honor, *this property is a safe harbor in an area of conflict*. And I've only been to the property one time, and that was the time that the Court visited the property. And if there was ever a true statement that a picture is worth a thousand words, a visit to this property was worth many days of testimony.

Your Honor, the City would ask the Court to confirm this Plan. If you consider the down side to Heartland, if the Plan does not work, they get to foreclose. They get exactly what they want. What we're asking for and what the Debtor is asking for is a chance. And this is the court of chance. Give us an opportunity to pay them the true value for this property and to give the citizens of Fort Worth what they bargained for when they invested the money in the project. Thank you.

Confirmation Hearing Transcript, Volume V, at 51-52 (emphasis added).

at 16. The Court of Appeals concluded that the relationship with the City was essential to the continued operation of the housing complex. *Id.* This holding is consistent not only with *Greystone* but also with the case law of other circuits.[12]

Accordingly, there is no conflict in the development of this doctrine in the lower courts; it is appropriate to leave to the lower courts the task of tailoring, on a case-by-case basis, the contours of the justification for separate classification.

Furthermore, even if this Court were inclined to consider the standards for separate classification in typical bankruptcies, the unique fact pattern makes this case a very poor vehicle for that purpose. The multiple roles occupied here by the City would rarely, if ever, reoccur in other cases; thus any ruling by this Court on separate classification of the City's claim in this unusual case

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[12] For example, separate classification of the City's claim allowed Briscoe to maintain an important, ongoing relationship with the City. *See In re LeBlanc*, 622 F.2d 872, 879 (5th Cir. 1980) (special relationship with creditor justified different treatment of similar claims). The City's commitment of $20,000 a month to provide tenant subsidies would arguably have been lost had the City's claim been classified with Heartland's unsecured claim. Other courts have also established that separate classification of similar claims is appropriate where interests other than payment of claims is involved. *In re U.S. Truck Co.*, 800 F.2d 581 (6th Cir. 1986) (separate classification permitted where future interests other than payment of debt were at stake). *In re Atlanta West VI*, 91 B.R. 620, 626 (Bankr. N.D. Ga. 1988) (separate classification of unsecured claim allowed for creditor providing an infusion of new funds under the plan).

would have little value as a guiding precedent.[13] Further, the particular facts in this case establish a separate ground to affirm the lower court's confirmation of Briscoe's Plan under the cramdown provision – a potential quagmire that has nothing to do with the classification issue presented for review.[14] These factual peculiarities would disqualify this case as a candidate for certiorari even if a conflict did exist between the circuits on standards for approving separate classification.

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[13] Indeed, after listing several grounds for concluding that the "city of Fort Worth is distinct from other creditors including Heartland" the Court of Appeals stated, "We emphasize the narrowness of this holding." 994 F.2d at 1167; Pet. App. at 16.

[14] Specifically, the classification issue centers on whether the City's unsecured Class 3 claim was properly classified as separate from Heartland's claim. The record establishes that Class 2 – the City's secured ad valorem tax claim – also voted affirmatively for Briscoe's Plan. Testimony of counsel for the City, Confirmation Hearing Transcript, Vol. III at 83. Even if the City's unsecured Class 3 claim had been improperly classified, the Class 2 vote would arguably qualify as an affirmative vote for the plan such that Briscoe could avail itself of the cramdown provisions. Response of Briscoe to Suggestion for Rehearing *En Banc* at 7-9. The appellate court never discussed this issue, so this Court might need to confront the outcome-determinative question whether the City's affirmative Class 2 vote qualified to trigger the cramdown provisions (which may or may not raise fact questions). Accordingly, after full briefing, the existence of the separate ground to affirm confirmation of Briscoe's plan could result in a decision that certiorari was improvidently granted. *See, e.g., The Monrosa v. Carbon Black, Inc.*, 359 U.S. 180 (1959) (granting of writ was improvident where judgment below was correct on a different ground).

CONCLUSION

None of the issues Heartland presents is worthy of review by this Court. Concerning the burden of proof (Point 1), the Court of Appeals Opinion applies this Court's precedent and does not conflict with any other circuit, but rather accords with a Tenth Circuit decision in this area of the law. With regard to Point 2, the Fifth Circuit did not shift the burden of proof to Heartland on the issue whether the Plan was fair and equitable. Finally, there is no circuit conflict on the classification issue presented by Heartland and the factual predicate for the ruling below on this issue is nonrecurring (Point 3).

For these reasons, this Court should deny Heartland's petition for writ of certiorari.

Respectfully submitted,

RALPH I. MILLER*
CRAIG H. AVERCH
RUTH L. RICKARD
WEIL, GOTSHAL & MANGES
100 Crescent Court, Suite 1300
Dallas, Texas 75201-6950
(214) 746-7700

Attorneys for Respondent
*Counsel of Record

WEIL, GOTSHAL & MANGES
A PARTNERSHIP INCLUDING PROFESSIONAL CORPORATIONS
100 Crescent Court
Suite 1300
Dallas, Texas 75201-6950
(214) 746-7700
Fax: (214) 746-7777

HOUSTON
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(SILICON VALLEY)
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WARSAW

WRITER'S DIRECT LINE
(214) 746-7740

March 31, 1993

VIA FEDERAL EXPRESS
Susan Vaughn, Case Manager
United States Court of Appeals
600 Camp Street
New Orleans, Louisiana 70130

Re: *Heartland Federal Savings and Loan Association v. Briscoe Enterprises, Ltd., II*
Case No. 92-1446

Dear Ms. Vaughn:

Briscoe Enterprises, Ltd., II ("Briscoe") submits the following in response to the Court's March 25, 1993 letter regarding this matter.

A. BURDEN OF PROOF

Briscoe agrees with Professor Warren's conclusion that the appropriate evidentiary burden of proof in a bankruptcy case in general, and in a contested confirmation hearing under section 1129(b) of the Bankruptcy Code in particular, is preponderance of the evidence. Professor Warren suggests that the bankruptcy power is subject to the Fifth Amendment takings clause under "unusual circumstances." That point, however, is the subject of debate. To the extent that the appropriate evidentiary standard depends on the constitutional status of a secured creditor's lien in a bankruptcy case, Briscoe would note to the Court that some commentators question whether the bankruptcy power is subject to the Fifth Amendment at all. *See* Rogers, *The Impairment of Secured Creditors' Rights in Reorganization: A Study of the Relationship Between the Fifth Amendment and the Bankruptcy Clause*, 96 Harv. L. Rev. 973, 1030-31 (1983); Carlson, *Postpetition Interest Under the Bankruptcy Code*, 43 U. Miami L. Rev. (1988). Professor Warren is correct that even if the takings clause is implicated in a bankruptcy case, the appropriate standard is the preponderance standard. To the extent the Fifth Amendment is not implicated, it is clear that preponderance is the proper standard for a contested confirmation hearing under section 1129(b).

This case does not involve any unusual circumstances that would require a stricter burden of proof. Rather, this case involves only a monetary dispute between a debtor and a secured creditor. There is absolutely no rational basis to raise the standard of proof beyond preponderance. Further, the Bankruptcy Code is

silent as to the applicable burden of proof. Because Congress did not include a burden of proof in the statute, the general preponderance of the evidence standard applicable to civil litigation is appropriate in this case. A stricter standard of proof is not warranted.

B. VALUE OF PROPERTY

Professor Warren correctly concluded that balloon payments are permissible, even when the source of funds for payment of the balloon is not determined at confirmation, so long as the bankruptcy court has concluded that the value of the property will not decline. Of course, the confirmed Plan in this case does not provide a balloon in the traditional sense. The principal balance of Heartland's secured claim is amortized during the term of the Plan. Approximately twenty-five percent (25%) of the principal balance of the secured claim will be paid by the end of the fifteenth year. While it is true that the Bankruptcy Court did not make a specific finding regarding the value of the Property fifteen years after confirmation, the Bankruptcy Court had before it credible evidence that the Property would not decline in value. The Bankruptcy Court considered the following factors:

a. Implementation of the Plan requires a minimum income of $200,000 per month. (Briscoe Exhibit 3; Tr. Vol. II, at pp. 87-88);

b. Briscoe had achieved income in excess of $200,000 per month at the end of 1990 and in early 1991, even while the Property was only 85% occupied. (Tr. Vol. II at pp. 83-84);

c. Briscoe will increase the rent on all 784 units by $5 per month beginning July 1991. As a

result, monthly income will increase to $260,000. (Briscoe Exhibits 1 and 2; Tr. Vol. II, at p. 84);

d. Occupancy at the Property is expected to increase substantially. (Tr. Vol. II, at pp. 75-83; Tr. Vol. III at 24);

e. With a minimum income of $200,000 per month, Briscoe can pay its operating expenses, debt service, *ad valorem* taxes and pay for some repairs not covered by the Insurance Proceeds. (Briscoe Exhibits 2 and 6; Tr. Vol. II at pp. 87-96);

f. Repairs (some of which are not immediate) will be made from Insurance Proceeds or net operating income. (Tr. Vol. II, at 104);

g. Turnover rates at the Property range from 25-30% as opposed to a common range of 64-104% in the Dallas/Fort Worth metropolitan area. (Tr. Vol. III, at pp. 21-25);

h. Briscoe has reduced vacancies from approximately 400 to approximately 50 during the case. (Tr. Vol. II at p. 84; at pp. 219-220);

i. The Bankruptcy Court judge visually inspected the Property (Tr. Vol. IV at pp. 156-163) and was impressed with its condition. (Tr. Vol. V at pp. 70-71);

j. Approximately $750,000 in *ad valorem* taxes will be paid prior to the end of the Plan term. (Tr. Vol. II at p. 120);

k. Briscoe will make monthly principal payments to Heartland with interest at the rate of 10.25% per annum. During the term of the Plan, approximately $1.7 million of principal

of Heartland's secured claim will be paid. (Tr. Vol. II, at pp. 121-123). Heartland did not object to the interest rate or the loan term.

l. The City of Fort Worth, throughout the confirmation hearing, supported the continuation of the Property as a safe, clean and affordable low to moderate income residential community. (Tr. Vol. V, at pp. 51-52).

Based on these and other factors, the Bankruptcy Court impliedly found that the value of the Property would remain constant or increase during the term of the Plan.[1] The Bankruptcy Court further found the Plan to be feasible based upon applicable law and this finding is not clearly erroneous. Had the Bankruptcy Court believed that the value of the Property would decline, or that Heartland would not be adequately protected, the Bankruptcy Court could not have found the Plan to be feasible. Consequently, the balloon payment required by the Plan is appropriate.

C. Motivation of the equity interests' efforts in this reorganization considering that its interests are extinguished.

This question can be addressed in two parts. First, Briscoe recognized and discharged its fiduciary duty to its creditors to promulgate a confirmable chapter 11 plan

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[1] *Texas Mortgage Servs. Corp v. Guadalupe Sav. & Loan Assn. (In re Texas Mortgage Servs. Corp.)*, 761 F.2d 1068, 1075 n.12 (5th Cir. 1985) (If a trial judge fails to make a specific finding on a particular fact, the reviewing court may assume that the court impliedly made findings consistent with its general holding).

that would maximize the return to *all* creditors of the estate. Including the undersecured claim of the City of Fort Worth, there are approximately $8 million of creditors (other than Heartland) that have an economic stake in this reorganization. (Tr. Vol. II, at pp. 120-122). The structure of the confirmed chapter 11 Plan allows the maximum recovery to unsecured creditors and ensures that Heartland will receive the present value of its secured claim. Put differently, the creditors, including Heartland, benefit if the Property performs as projected. If the Property fails to perform as projected, however, Heartland will recover its security.

Second, and perhaps most important to Briscoe, Briscoe desires to accomplish a reorganization that will be socially responsible. The Property is not a typical apartment complex. The Property essentially is a 784 unit quasi-public residential community in which the City of Fort Worth invested $7 million for construction. The objective of Briscoe and the City of Fort Worth in constructing the Property was to provide clean, secure, and affordable housing for low to moderate income families residing in an otherwise inhospitable part of Fort Worth, Texas. The Property is located in a high crime and drug traffic area of Fort Worth. Approximately ninety percent (90%) of the residents are African-American, most of whom are single female heads of household. (Tr. Vol. II at pp. 59-62).

The Property offers many desirable amenities that often are not found in low income communities. The Property provides residents with 24-hour security, staffed by at least two security guards at all times, an on-site daycare center, playgrounds, club rooms, swimming

pools, tennis courts, basketball courts, and a video game room. (Tr. Vol. II at p. 61). Crime, while rampant in the surrounding community, is almost non-existent in the Property itself. It is for these and other similar reasons that the City of Fort Worth has supported Briscoe's prior ownership of the Property and the chapter 11 Plan. Neither Briscoe nor the City of Fort Worth have ever been provided any assurance that Heartland would, in the event of a foreclosure, be sensitive to the needs of the residents or maintain the quality and integrity of the Property.

A trust was created under the Plan to ensure the continued viability of the community created by Briscoe and supported by the City. Two of the trustees of the trust created under the Plan will be appointed by the two largest holders of claims represented in the trust – Heartland (holding an approximately $10 million undersecured claim) and the City of Fort Worth (holding an approximate $8 million claim). Because over 90% of the residents of the property are African Americans, and to ensure proper stewardship for the residents and the Property, one trustee will be appointed by the NAACP to represent the community's interests. The mandate of the trust is clear: maintain the quality and integrity of the property for the tenants and surrounding community.

Certainly, the equity owners of Briscoe desired to retain ownership of the Property. Unfortunately, it became clear at the commencement of this bankruptcy case that the equity owners of Briscoe did not have the financial ability to contribute any significant capital to the reorganization effort. Consequently, all thoughts relating to a "new value" plan were quickly replaced with the two

goals discussed above. The equity owners constructed and operated the Property not only to make a profit, but also as a humanitarian and philanthropic endeavor to enhance the lives of others. Consequently, the equity interests remain committed to doing whatever it takes to maintain the Property as a showcase of a premier low-income housing community in the City of Fort Worth.

The purpose of this chapter 11 case was to forge a consensual plan of reorganization. Often, bargains are made under the shadow of the Bankruptcy Code. By creating a "confirmable" chapter 11 plan, the Debtor hoped to foster a negotiated resolution with its most (and only) recalcitrant creditor – Heartland. This strategy, of course, while consistent with the language, spirit, and purposes of the Bankruptcy Code, proved to be unsuccessful in this case. Briscoe looks forward to the Court's ruling in this matter.

Sincerely,

/S/

MARILYN D. GARNER

MDG/ms
cc: Douglas S. Lang
L. Edward Briscoe
Joseph Colvin